

**IN THE MATTER OF THE APPLICATION REGARDING CONVERSION  
OF PREMIERA BLUE CROSS AND ITS AFFILIATES**

Washington State Insurance Commissioner's Docket # G02-45

**PRE-FILED DIRECT TESTIMONY OF:**

**Kent S. Marquardt**

Executive Vice President and Chief Financial Officer  
Premiera Blue Cross

March 31, 2004

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**Introduction**

**Q. Please state your name.**

A. Kent S. Marquardt.

**Q. Please state your employer, title, and business address.**

A. I am Executive Vice President and Chief Financial Officer of Premera Blue Cross. Premera is located at 7001 – 220th Street S.W., Mountlake Terrace, Washington.

**Credentials**

**Q. Would you briefly describe your professional background?**

A. I started my career in public accounting with the accounting and consulting firm KPMG Peat Marwick where I was employed for 19 years and admitted to the partnership in 1988. I started in the audit practice in the Milwaukee office in 1976, moved to the Phoenix office in 1985, and then to the Long Beach, California office in 1991. I began focusing on healthcare consulting in 1988, dealing principally with hospitals and physician groups.

In 1995 I joined PriMed Management as its Chief Financial Officer. I then moved to MedPartners, a publicly traded company, as its Chief Financial Officer for Western Operations in 1996. After a year and one-half in that position I became MedPartner's Chief Operating Officer for Western Operations. In 1998 I joined a start-up company called American Dental Specialists, which was ultimately unsuccessful in attracting sufficient venture capital. I joined Premera Blue Cross as Chief Financial Officer in October of 1998.

1 **Q. What are your responsibilities as Executive Vice President and Chief**  
2 **Financial Officer of Premera?**

3 A. I am responsible for the Premera family of companies' finance, actuarial, business  
4 information services, underwriting and healthcare economics departments.

5 **Q. Were any of the companies you worked for for-profit or publicly traded**  
6 **companies?**

7 A. KPMG is a for-profit partnership. Both PriMed Management and American  
8 Dental Specialists were for-profit, nonpublic companies. MedPartners was a for-profit,  
9 publicly traded company.

10 **Q. Are you a member of any professional societies or associations?**

11 A. I'm a member of the American Institute of Certified Public Accountants, the  
12 Wisconsin Society of Certified Public Accountants and the California Society of  
13 Certified Public Accountants.

14 **Q. Aside from Premera and any professional societies or associations, are there**  
15 **any other organizations in which you have been recently active?**

16 A. I am on the board of the Economic Development Council of Snohomish County.

17 **Q. Please describe your educational background.**

18 A. I received a Bachelor of Business Administration from the University of  
19 Wisconsin at Whitewater, and a Master's in Business Administration from the University  
20 of Wisconsin at Madison.

21 **Form A Statement**

22 **Q. Are you familiar with the Form A Statement filed with the regulators in**  
23 **connection with the proposed conversion of Premera and certain of its**  
24 **affiliates to for-profit corporation status?**

A. Yes, I am. On September 17, 2002, Premera filed a "Statement Regarding  
Acquisition of Control of a Domestic Health Carrier and Domestic Insurer" ("Form A

Statement”). Premera supplemented the Form A Statement on September 27, 2002, and October 25, 2002, and amended it on February 5, 2004.

**Risk Based Capital (RBC) and Premera’s Current Capital Position**

**Q. In general, how does a health plan evaluate its capital position?**

A. A health plan’s statutory capital is its assets minus liabilities and obligations, as defined by statutory accounting principles. A health plan must have an appropriate level of statutory capital to allow the organization to withstand losses due to unexpected fluctuations in the cost of medical claims. Without this protection, policyholders may experience service disruptions such as unpaid claims.

The National Association of Insurance Commissioners (“NAIC”) developed a standard formula to determine the minimum level of statutory capital needed for protection from insolvency. This minimum level of statutory capital, or Authorized Control Level, is based on an organization’s size, structure and retained risk. There are several factors that go into the calculation, including the risk of underwriting the business, asset risk, credit risk, other business risk, and affiliate risk.

The Authorized Control Level of statutory capital calculated from the formula is compared to the actual adjusted statutory capital held by the organization, with the result being generally referred to as the Risk Based Capital level (“RBC”) of the company. If the actual adjusted statutory capital is higher than the minimum level, then the company passes the minimum capital adequacy test. Meeting this minimum requirement, however, does not mean that the organization is financially sound.

If actual adjusted statutory capital is at or below a certain trigger point, then the company is subject to regulatory action by the state. RBC must be over 200% to avoid

1 such regulatory intervention. At a level below 200% the insurance commissioner has  
2 regulatory oversight of the company's corrective action plans for raising its capital above  
3 the 200% threshold. At an RBC of 100% the insurance commissioner is authorized to  
4 take whatever regulatory action is necessary, including taking control of the company, to  
5 protect the interests of policyholders.

6 The Blue Cross Blue Shield Association ("BCBSA") has its own, more stringent,  
7 RBC trigger points. If RBC falls below 375% of minimum statutory capital, a plan is  
8 subject to special BCBSA monitoring and reporting obligations. At 200% of RBC the  
9 BCBSA is authorized to strip a health plan of its right to use the Blue names and marks.

10 A more complete discussion of the NAIC risk-based capital formula structure is  
11 presented in Appendix A to the report by NovaRest Consulting titled "Capital  
12 Requirements and Sources of Capital" dated November 10, 2003, and filed in this matter  
13 ("NovaRest Report").

14 **Q. Why are the Blue Cross Blue Shield Association requirements more stringent**  
15 **than state regulatory standards?**

16 A. My understanding of the reason for the more stringent BCBSA standard is that the  
17 association believes that a higher standard is appropriate for financial soundness and  
18 protection of the Blue brand. The Blue brands stand for, among other things, safety and  
19 security. If one Blue plan is subject to regulatory intervention because of inadequate  
20 capital, it reflects negatively on the Blue Cross Blue Shield Association and all Blue  
21 Cross and Blue Shield plans. The BCBSA's more stringent requirements allow it to  
22 monitor performance and require corrective actions before a plan gets into regulatory  
23 trouble.  
24

1 **Q. Does the association have an arrangement to contribute to any Blue plan that**  
2 **is in trouble?**

3 A. No, it does not. Each Blue plan is an independent licensee of the BCBSA. Each  
4 Blue plan is a separate and distinct entity from the BCBSA and other non-affiliated plans.

5 **Q. What is Premera's current capital position?**

6 A. At the end of 2003, Premera's RBC was 433 percent.

7 **Q. How does that RBC level compare to other Blues around the country?**

8 A. Premera's RBC level is in the bottom quartile of all of the Blues in the country  
9 which disclose their RBC level. The Blues system-wide average was 664 percent at June  
10 30, 2003.

11 **Q. What would Premera's preferred capital position be?**

12 A. We believe an RBC of 500 to 600 percent would provide Premera with capital  
13 flexibility.

14 **Q. And would that range be achievable if Premera was a public company?**

15 A. Yes. If we receive approximately \$100 - \$150 million through an equity offering,  
16 our capital level would be within our preferred range.

17 **Q. What can negatively impact a company's RBC?**

18 A. RBC is the level of actual statutory capital relative to the minimum statutory  
19 capital level as defined by the NAIC. Anything that decreases actual statutory capital or  
20 increases the Authorized Control Level of statutory capital negatively impacts RBC.  
21 Actual statutory capital is decreased primarily through operating or investment losses and  
22 investments in non-admitted assets, which include for example information technology  
23 and pre-paid pension cost. On the other side of the ledger, the requirements for minimum  
24 statutory capital move higher as membership grows. As the company takes on more

1 members, it takes on more risk, and it must either increase its statutory capital level or  
2 suffer diminished RBC.

3 Please see the NovaRest Report for a fuller discussion of how capital can be  
4 impacted, the need for capital, sources of capital, affordable growth and the implications  
5 of being capital constrained.

6 **Q. Has Premera fallen below the BCBSA early warning levels in the last several**  
7 **years?**

8 A. In 1998 Premera was below the BCBSA early warning threshold, under the old  
9 capital benchmark system, after experiencing losses in the mid-1990's in the market for  
10 individual products. At year-end 1999 the company's capital position had improved and  
11 its RBC was above the early warning threshold of 375%. As of December 31, 2003,  
12 Premera's RBC was 433%.

13 **Q. Have you read the report from the Milliman USA titled "Premera**  
14 **Comparative Premium Rate Analysis" dated November 10, 2003, and filed in**  
15 **this matter ("Milliman Report")? If so, do you have any comments or**  
16 **observations on that report related to RBC?**

17 A. The Milliman Report, which notes that a company needs adequate capital to  
18 weather business ups and downs, supports the position that Premera should augment its  
19 capital to reach a more appropriate capital level.

#### **Conversion Rationale**

20 **Q. Why is Premera undertaking this conversion?**

21 A. The principal reasons for undertaking this conversion are to provide capital to  
22 enhance the company's capital position, position the company for growth in membership,  
23 and provide funds for investment in infrastructure and products. For the last several  
24 years the company has been capital constrained. That limits our ability to grow

1 membership and remain competitive. As Chief Financial Officer, I have worked with  
2 Premera's Board of Directors to explore various options for increasing our capital. The  
3 Board has concluded that becoming a public company is the best option to provide capital  
4 and financial flexibility for Premera. Our vision is to become the health plan of choice  
5 and the standard of excellence in our service areas. As we succeed and our membership  
6 grows, we will have a recurring need for additional capital. Access to equity capital will  
7 enable us to achieve that vision.

8 **Q. What are the primary options for obtaining additional capital as a non-**  
9 **profit?**

10 A. Premera's main options for obtaining additional capital as a non-profit, other than  
11 affiliating or merging with another company, are internally generated funds (*i.e.*, profits),  
12 the sale of assets, debt financing, or some combination thereof. Some of these options  
13 are one-time in nature, and none of them provide adequate capital or financial flexibility.  
14 These options are more fully described in Exhibit E-7 of the Form A Statement and in the  
15 NovaRest Report.

16 **Q. One of the sources of capital you mentioned was growing profits. What are**  
17 **the constraints that Premera faces with augmenting its capital position by**  
18 **raising premium rates?**

19 A. We cannot increase our profit margin simply by increasing premium rates.  
20 Premium rates are determined primarily by competition. The health insurance market in  
21 Washington is competitive and we must charge competitive rates or risk losing  
22 membership. We know this from our own experience. Our historic strength has been in  
23 the small employer and individual markets, both of which are very price sensitive. When  
24 our rates have exceeded those of our competitors, customers have left Premera to join  
lower priced health plans. Premera's expert economists, National Economic Research

1 Associates (“NERA”), confirm that the market for the sale of health insurance in  
2 Washington is competitive. Thus the market itself limits Premera’s ability to increase  
3 profits by charging higher rates.

4 **Q. Why is Premera seeking access to capital markets now when you have**  
5 **already funded a major corporate initiative like Dimensions?**

6 A. Dimensions is an innovative business platform and suite of products that we  
7 believe is responsive to customer demands. It therefore positions Premera for strong  
8 membership growth. To the extent we add members, however, we will put continued  
9 strain on our capital position. We need additional capital flexibility to support that  
10 growth.

11 In addition, the implementation of Dimensions was a significant and expensive  
12 undertaking, but our capital investments don’t stop there. The Dimensions platform will  
13 need continued investments to enhance e-business capabilities, enhance service  
14 efficiencies, continue to improve system interfaces and stream-line processes. There is a  
15 continuous need for additional investment to serve our members and operate efficiently  
16 with our network physicians and hospitals. Alan Smit, Premera’s Chief Information  
17 Officer, has provided testimony on technology investments that will need to be made.

18 **Q. How has Premera funded its previous capital expenditures, Dimensions**  
19 **being one recent example, and why can’t Premera fund future investments in**  
20 **infrastructure in the same way?**

21 A. Some capital expenditures have been financed by ongoing profits, but as I said  
22 earlier, profits at our current and anticipated margin levels are not sufficient to fund  
23 significant new investment. Premera financed the Dimensions project through a series of  
24 sale-and-leaseback transactions over the last three years. However, funding future  
investments in this way has significant limitations. Sale-and-leaseback transactions are

1 limited to tangible assets and cannot be used to fund non-tangible infrastructure  
2 improvements.

3 **Q. Did you consider what could happen to Premera's capital position under**  
4 **various possible scenarios?**

5 A. Yes. We tested what would happen to our capital position considering various  
6 future scenarios. We looked at the impact of positive developments like stronger than  
7 expected success in attracting new members. We also considered the effects of possible  
8 negative developments like a downturn in the stock market.

9 As part of our analysis, we looked at how our financial projections might change  
10 under four different sensitivity scenarios. These scenarios were modeled so we could  
11 understand the impact of the assumed conditions or events on Premera's capital position.

12 We wanted to use realistic scenarios. Therefore, each of the scenarios was based  
13 on events and conditions Premera had previously experienced. The first scenario  
14 considered increased membership growth over that contained in the Form A Statement  
15 financial projections. The second scenario included a small acquisition. The third  
16 scenario projected what would happen if Premera's operating margins were lower than  
17 originally planned. The fourth scenario presented financial results if investment returns  
18 turned out lower than expected.

19 Again, the purpose of each of these scenarios was to analyze the impact of certain  
20 circumstances on Premera's capital position and to test how much capital flexibility  
21 Premera possesses. We then compared the impacts as a non-profit entity and as a for-  
22 profit corporation with access to equity capital.  
23  
24

1 **Q. What did you conclude from testing those scenarios?**

2 A. In our current non-profit form, any one of these events would result in a reduction  
3 of Premera's Risk Based Capital by 50 to 75 points because we do not have another  
4 source of capital. That would reduce RBC to the 350 - 375 level. As I discussed earlier,  
5 that falls below the BCBSA early warning threshold. By contrast, as a public company  
6 Premera would possess capital flexibility to maintain its RBC level in spite of downturns  
7 in investment and operating income, or increased capital requirements resulting from  
8 membership growth. Becoming a public company would make Premera a stronger  
9 company capable of both withstanding economic downturns and capitalizing on market  
10 opportunities.

11 **Q. Is the conversion reorganization, in your view, in the best interests of the  
12 policyholders, and if so, how?**

13 A. Yes. We believe a conversion is in the best interests of policyholders. A  
14 conversion will enhance our ability to provide customer support, to build service  
15 capabilities, and to invest in infrastructure which are all required to provide outstanding  
16 value to our customers. It will also make Premera a more financially secure company.  
17 We are ensuring that our coverage will be there when our members need it.

18 **Premera as a Public Company**

19 **Q. How does Premera currently compare with publicly traded health plans, as a  
20 general matter?**

21 A. The publicly traded companies providing health care coverage are diverse. Some  
22 are extremely large national companies; a few are small or mid-size regional carriers; and  
23 some are specialized carriers, such as those serving Medicaid enrollees. We are most  
24

1 similar to the small to mid-size regional carriers, such as WellChoice, Oxford, Coventry  
2 Health Corporation, Sierra Health Plan, and Healthnet.

3 **Q. How do Premera's projections fit with Wall Street expectations?**

4 A. From an operating margin standpoint, we are currently on the low end of the scale  
5 when compared to other publicly traded health plans. However, we have received  
6 investment banker and analyst advice that Premera will be valued on, among other  
7 attributes, its prospects for continued margin improvement and continued operating  
8 income growth. Our financial projections of 20 percent annual growth in operating  
9 income and 15 percent annual growth in net income fit well within the market's  
10 expectations.

11 In its report titled "Opinions as to Market Acceptance and Issues Related to the  
12 Proposed Conversion of Premera Blue Cross," dated November 10, 2003, and filed in this  
13 matter ("BAS Report"), Banc of America Securities concludes "Premera's rationale and  
14 metrics should satisfy investor expectations, taking into account past trends and current  
15 market conditions, and therefore, be viewed as an attractive investment."

16 **Q. What internal changes will Premera have to make once it is public, in terms  
17 of, for example, staff reporting requirements or Sarbanes-Oxley?**

18 A. We are already in the process of implementing many of the relevant provisions of  
19 Sarbanes-Oxley as a best practice, and that won't change whether we go public or not.  
20 There will be additional public reporting requirements to the SEC, but those, and the  
21 other internal changes resulting from becoming a public company, are within our  
22 capabilities.  
23  
24

1 **Q. What drives the value of publicly traded companies?**

2 A. Value is driven by both qualitative and quantitative characteristics of a company.  
3 Qualitatively, as the BAS Report states, investors will value Premera on whether it  
4 “provides high quality healthcare insurance products and services, builds and maintains  
5 strong provider networks, makes sound underwriting decisions, is in good standing with  
6 regulatory authorities, has effective product design and, most importantly, possesses a  
7 highly satisfied customer base that believes Premera adds significant value.”  
8 Quantitatively, value is driven by demonstrating an ability to make consistent  
9 improvements in operating and financial performance over time. In our case, metrics  
10 such as revenue growth, operating income growth and net income growth, are key drivers  
11 of value.

12 **Q. Others have asserted that as a result of conversion Premera as a for-profit**  
13 **will seek to maximize profits by increasing revenues and decreasing costs. Do**  
**you agree?**

14 A. I disagree. Whether we are non-profit or for-profit, we will need to continue our  
15 drive to be financially sound by setting objectives to grow operating income and net  
16 income and controlling costs. We operate in a competitive market. We cannot simply  
17 raise rates and hope to retain business, or lower provider reimbursement and expect  
18 providers to remain in our networks.

19 **Q. Others have suggested that shareholder pressure would cause Premera to**  
20 **reduce the benefits it offers and its service levels. What's your response?**

21 A. To the contrary, we are seeking to convert to gain access to capital to improve our  
22 products and services. Our business strategy is dictated by customer expectations and  
23 market demands, not by the capital structure of the company. As stated above, BAS  
24

1 reports that investors look to qualitative as well as quantitative characteristics of a  
2 company. Our value proposition is high quality service and products.

3 **Form A Financial Projections**

4 **Q. Was there any change to the Form A Statement financial projections as part**  
5 **of the Form A Statement amendment filed on February 5, 2004?**

6 A. No, there was not. We have, however, provided the state consultants as part of  
7 their due diligence with actual financial results through year-end 2003 and other financial  
8 data.

9 **Q. Focusing then on the original Form A Statement financial projections, were**  
10 **you primarily responsible for the development of those financial projections?**

11 A. Yes, I was.

12 **Q. What were the primary assumptions used to develop the Form A Statement**  
13 **financial projections?**

14 A. The major assumptions used to develop the Form A financial projections are  
15 related to growth of membership, healthcare cost trends, premium levels, and general and  
16 administrative costs. We assumed, for example, that we would be able to price our  
17 business to cover healthcare cost trends and maintain our medical loss ratio within an  
18 approximate 84 percent range. The assumptions are explained in more detail in Exhibit  
19 E-7 of the Form A Statement.

20 **Q. How far out did these projections go?**

21 A. They are five-year projections, as required by the state.

22 **Q. How would you characterize the financial projections filed in the Form A**  
23 **Statement?**

24 A. The Form A financial projections are a reasonable forecast of what we expect to  
happen over the next five years. As stated in the Form A Statement, the underlying  
assumptions used in developing the financial projections are consistent with Premera's

1 strategy, current market trends, and management's estimates of the financial results  
2 associated with the implementation of its strategy.

3 Obviously, anytime you look out over five years, there are a lot of things that can  
4 and will change during that period which could cause actual results to be different than  
5 the forecast as explained more fully in Exhibit E-7 of the Form A Statement.

6 **Q. Did Premera's Board of Directors review and approve the Form A Statement**  
7 **financial projections that were submitted?**

8 A. Yes, they did.

9 **Q. Was more detailed information underlying the Form A Statement financial**  
10 **projections provided to the state consultants?**

11 A. Yes, a detailed financial model was provided to the state consultants that provides  
12 projections by line of business.

13 **Q. Are the Form A financial projections the same financial information that will**  
14 **be provided to Wall Street, and if not, how and why do they differ?**

15 A. No. Wall Street would not receive financial projections covering a five-year  
16 period. Consistent with Wall Street expectations, prior to the IPO we would provide  
17 investors with guidance as to what we expect to achieve financially over the next year.  
18 Our guidance would include such metrics as revenue, operating margins, operating  
19 income, and net income.

20 **Q. In general, how did the process of preparing financial projections for the**  
21 **Form A Statement compare with the type of financial planning that you do**  
22 **normally for your company?**

23 A. It was similar. The Form A Statement financial projections look out for a longer  
24 period than we traditionally use for detailed financial planning.

1 **Q. Would the Form A financial projections be the same if Premera was not**  
2 **undertaking a conversion?**

3 A. Yes.

4 **Managing Premera's Portfolio of Businesses**

5 **Q. Premera "manages lines of business as a portfolio." Could you tell us what**  
6 **that means?**

7 A. We think of our lines of business as an investment portfolio, where the key to  
8 investment success is the proper diversification of assets. Diversification means more  
9 than just having different types of investments. It means having a mix of investments  
10 across sectors, markets, instruments and so on.

11 When you diversify your investments, you spread your money among many  
12 different securities, thereby avoiding the risk that your portfolio will be badly affected  
13 because a single security or a particular market sector fails to perform. By diversifying  
14 across assets, you can reduce your risk without necessarily having to reduce your returns.  
15 That is, if you have a diversified portfolio your overall portfolio risk will be lower.

16 Premera's portfolio of lines-of-business is diversified geographically and by  
17 product. Geographically we have been offering healthcare coverage in three states, and  
18 just began offering such products in Arizona as well. Our product line is diversified  
19 across individual, small-group, large-group, and self-funded businesses. In any given  
20 year, some of our markets and products will hit or exceed their financial targets, and  
21 some will not. Overall, however, diversification allows us spread our risk and reach our  
22 financial goals in the aggregate.  
23  
24

1 **Q. Does the objective of focusing on profitable growth have anything to do with**  
2 **whether or not you're a for-profit or not-for-profit company?**

3 A. No, it does not. Ultimately, it has to do with remaining a strong company. No  
4 health plan, or any company for that matter, can survive long term if it isn't profitable.

5 **Q. Do you expect all lines of business to meet financial expectations at all times?**

6 A. No, we do not.

7 **Q. A PricewaterhouseCoopers report filed in this case says that high-**  
8 **performing companies expect all lines of business to meet expectations at all**  
9 **times. Do you agree with that statement?**

10 A. To be a successful public company you generally meet overall expectations. In  
11 setting overall expectations, I don't believe any company expects every single line of  
12 business to operate at peak performance at all times. A line of business may not be  
13 profitable for some period of time, but we may decide to stick with it because it helps  
14 cover our costs and because we have developed a plan to restore it to profitability.

15 **Taxes**

16 **Q. Will the transactions contemplated in Premera's Form A Statement be**  
17 **subject to federal tax?**

18 A. Based on current federal tax laws, the transaction will not trigger any gain or loss  
19 under federal income tax laws.

20 **Q. What assurances have you received that these transactions will not be**  
21 **taxable?**

22 A. We have engaged Ernst & Young to provide tax opinions on these transactions.  
23 Their draft tax opinions indicate that the conversion should be treated as a series of tax-  
24 free transactions for federal income tax purposes. Ernst & Young is expected to provide  
final opinions prior to the Form A hearing as provided in the Plan of Conversion  
submitted with the Form A Statement.

1 **Q. Have the OIC staff's consultants disagreed with Ernst & Young's**  
2 **conclusion?**

3 A. PwC expressed no opinion on the tax free treatment of the reorganization, but did  
4 state that it would "not be unreasonable" (in other words reasonable) to rely upon the  
5 Ernst & Young opinions that the transaction should be a tax-free reorganization for  
6 Premera.

7 **Q. There are certain tax deductions that Premera currently takes under Code**  
8 **section 833(b), are there not?**

9 A. That's correct. We believe we will be able to maintain those deductions under  
10 833(b). Ernst & Young has expressed, in a draft opinion, the view that it is "more likely  
11 than not" that Premera will maintain the 833(b) deduction in the context of the Premera  
12 conversion.

13 If we were to lose that deduction, which we don't believe we will, we have certain  
14 tax attributes, such as minimum tax credits and net operating loss carry-forwards, that  
15 would approximate our current tax rate through 2007 based on our financial projections.

16 **Q. Do you expect that the conversion will result in what's called an "ownership**  
17 **change" for purposes under Code Section 382?**

18 A. No, we do not. Ernst & Young's draft opinion states that the conversion "should  
19 not" result in an ownership change, at the time of the transaction, for tax purposes.

20 **Q. Have the OIC staff consultants disagreed with Ernst & Young's conclusions**  
21 **in that area?**

22 A. PwC expressed no opinion on the tax treatment of the reorganization, but did state  
23 that it would "not be unreasonable" (in other words reasonable) for Premera to rely upon  
24 the Ernst & Young opinion regarding the applicability of Code Section 382 to the  
conversion transaction.

1 **Q. Do you expect that Premera will undergo what's called an "ownership**  
2 **change" for tax purposes down the road?**

3 A. It is possible. If in the third year after the IPO more than 50 percent of the stock  
4 is sold, it could trigger a material change in ownership.

5 **Q. What do you believe is the likelihood of that occurring?**

6 A. I think it's possible. As we've looked at Ernst & Young's analysis, we don't  
7 believe that it would have a material impact on our tax position. PricewaterhouseCoopers  
8 has looked at this issue and agrees with the assessment that it should not have a material  
9 tax impact.

10 **Q. What state tax consequences, if any, do you expect that the conversion will**  
11 **have?**

12 A. We do not believe there will be any material Washington state tax consequences  
13 from the transaction. We do not believe there would be an imposition of Washington  
14 Business & Occupation tax, sales or use tax, or real estate excise tax.

15 **Q. Is Premera planning to seek a ruling to that effect from the Washington State**  
16 **Department of Revenue?**

17 A. Yes, we are.

18 **Q. Please highlight the major changes contained in the most recent Form A**  
19 **Statement amendments.**

20 A. The original Form A filing proposed a single foundation shareholder which would  
21 receive the initial stock on conversion and distribute the proceeds from the sale of that  
22 stock to two charitable organizations, one for Washington and one for Alaska. The  
23 current filing would establish two foundations, one for Washington and one for Alaska.  
24 These foundations would receive an allocated portion of the initial stock, sell the stock,

1 and use the proceeds for charitable purposes. This structural change was made at the  
2 insistence of the state consultants.

3 **Q. What is the tax effect of these structural changes?**

4 A. Our desire was to have the recipient of the stock qualify as a 501(c)(4), tax  
5 exempt organization, rather than a 501(c)(3) organization. The reason was to avoid the  
6 foundation incurring an excise tax on the value of the stock transferred to it. Such excise  
7 taxes could be in the \$5 million range, if imposed. Under the new structure, it remains  
8 the intent that the two foundations would also qualify for 501(c)(4) status and thereby  
9 avoid the excise tax and other taxes imposed on the operations of 501(c)(3) corporations.  
10 We preferred the original structure, but made the change because the state consultants  
11 required it.

12 **State Consultant Reports**

13 **Q. Have you read the OIC Consultant's final and supplemental reports filed in  
14 this matter?**

15 A. Yes, I have. The OIC Staff retained various consultants to review Premera's  
16 Form A Statement, namely, (i) an antitrust consultant, Dr. Keith Leffler, Ph. D., ("OIC  
17 Antitrust Consultant"); (ii) economic and actuarial consultants from  
18 PricewaterhouseCoopers ("PwC Economic Consultants"); (iii) executive compensation  
19 consultants from PricewaterhouseCoopers ("PwC Compensation Consultants"); (iv)  
20 accounting and tax consultants from PricewaterhouseCoopers ("PwC Tax Consultants");  
21 (v) investment banking consultants from The Blackstone Group ("Blackstone"); and (vi)  
22 the law firm of Cantilo & Bennett, L.L.P. ("C&B"). For ease of reference I will identify  
23 each final report filed on or about October 27, 2003, as the "initial" report. Collectively  
24 these reports will be referenced as "OIC Consultant Initial Reports." Each supplemental

1 report filed on or about February 27, 2004, will be referred to as the “supplemental”  
2 report, and collectively as “OIC Consultant Supplemental Reports.” Both reports of an  
3 OIC Consultant taken together will be identified as that consultant’s “Reports.” For  
4 example, the reports of Blackstone are identified as the Blackstone Initial Report and the  
5 Blackstone Supplemental Report, and together as the Blackstone Reports.

6 Cost Allocation

7 **Q. The PwC Economic Consultants state in their Supplemental Report that they**  
8 **believe it is important that Premera be able to accurately measure the cost of**  
9 **all Washington-based stand alone business units. Is Premera able to**  
10 **accurately measure the cost of stand alone business units?**

11 A. Yes. Premera does accurately measure the cost of all its stand alone business  
12 units. The actual costs incurred by Premera are assigned to each line of business by  
13 Premera’s cost accounting system. As a contractor to the federal government, Premera is  
14 subject to the Federal Acquisition Regulations. These require Premera to comply with  
15 regulations promulgated by the Cost Accounting Standards Board and to consistently  
16 follow its cost accounting practices. Because it follows those practices, Premera’s cost  
17 accounting system appropriately measures the cost of each of its lines of business.  
18 Neither Premera’s auditors nor PwC have expressed concern about Premera’s cost  
19 accounting system or methodology.  
20  
21  
22  
23  
24

Plan of Conversion

1  
2 **Q. Page 7 of the Blackstone Supplemental Report states: “The Washington**  
3 **Foundation and the financial advisor to the OIC should receive the**  
4 **preliminary proposal detailing the proposed IPO parameters (size, pricing**  
5 **range, split between primary and secondary shares) from Premera and its**  
6 **advisors at least 4 weeks prior to the commencement of the IPO roadshow.”**  
7 **How do you respond?**

8 A. Premera has no objection to providing the Washington Foundation and the  
9 financial advisor to the OIC a preliminary proposal detailing the proposed IPO  
10 parameters from Premera and its advisors at least four weeks prior to the commencement  
11 of the IPO roadshow. The Plan of Conversion, as filed, allows for such information  
12 sharing. If the state consultants believe the Plan of Conversion should expressly include  
13 language to the effect that Premera should supply such information at least four weeks  
14 prior to the commencement of the IPO roadshow, Premera would not object. A technical  
15 correction in the form provided in Exhibit A attached hereto, should eliminate the  
16 concern stated by the state consultants if approved by the Commissioner.

17 **Q. Page 7 of the Blackstone Supplemental Report related to the Plan of**  
18 **Conversion Section 4.3 states: “The Plan of Conversion should include the**  
19 **IPO as a closing condition for the overall Transaction.” How do you**  
20 **respond?**

21 A. Blackstone states that it is concerned that the fairness of the transaction  
22 could be adversely affected if the effectiveness of the IPO (*i.e.*, settlement of the IPO)  
23 does not occur at the same time as the conversion of Premera from a non-profit to a for-  
24 profit entity. Blackstone’s concern appears to be that the settlement (*i.e.*, payment for  
and transfer of common stock) of the IPO might not occur after the conversion. But the  
concern is unfounded. Premera intends for the conversion and IPO to occur  
simultaneously.

1           The Plan of Conversion states that the closing of such Conversion shall occur on a  
2     date to be determined by PREMERA upon fulfillment or waiver of specified conditions.  
3     That date is the Closing Date. Section 5.3 of the Plan of Conversion provides “[o]n the  
4     Closing Date, New PREMERA and/or the Foundation Shareholder will offer and sell to  
5     the public shares of Common Stock.” Therefore, Premera believes the Plan of  
6     Conversion, read in its entirety, provides what all the parties anticipate. Namely, that the  
7     IPO shall occur on the same day as the conversion of Premera.

8           If the state consultants continue to believe that there is an ambiguity, a technical  
9     correction in the form provided in Exhibit A attached hereto should eliminate the concern  
10    stated by the state consultants if approved by the Commissioner.

11   **Q.     Page 7 of the Blackstone Supplemental Report, related to the Plan of**  
12   **Conversion Section 4.3(b)(i), states that the window to complete an IPO after**  
13   **receiving all regulatory approvals should be twelve months and that the**  
14   **automatic three-month extensions should be removed. How do you respond?**

15    A.     Blackstone reasons that “[t]welve months represents an adequate window for  
16    Premera to complete an IPO based on a consideration of prior conversions and the  
17    potential for equity market dislocations.” Premera agrees that 12 months is adequate to  
18    address equity market dislocations. But that is not the reason for the two, three-month  
19    extensions. Section 4.3(b)(i) of the Plan of Conversion provides, in part,  
20    “Notwithstanding the foregoing, in the event there is any pending litigation related to the  
21    Conversion on the Closing Date, the 12-month period set forth above shall be extended  
22    by up to two successive three (3) month periods and, in addition, any approval period  
23    may be extended at the discretion of the Washington Insurance Commissioner and the  
24    Alaska Division of Insurance.” (Emphasis added.) Pending litigation related to the  
Conversion, if it occurs, could easily extend past the twelve month window. If no such

1 litigation occurs, or if it is disposed of within twelve months of receiving the approvals,  
2 then the automatic extensions cannot be invoked and the only extension possible is at the  
3 discretion of the Washington Insurance Commissioner and the Alaska Division of  
4 Insurance. The inclusion of the two, three-month automatic extensions for pending  
5 litigation, among other things, avoids creating a perverse incentive for those wishing to  
6 challenge the conversion to drag out the resolution of their claims.

7 **Q. The C&B Supplemental Report states that if the Washington Foundation**  
8 **does not have the ability to access, and rely upon, the information analyzed**  
9 **in the IPO Procedures Opinion, then the Washington Foundation should**  
10 **have the ability to appoint a joint bookrunning manager. How do you**  
11 **respond?**

12 A. There is no restriction on the OIC in the Form A Statement on providing the  
13 information analyzed in the IPO Procedures Opinion to the Washington Foundation. In  
14 the event the Commissioner concludes that specific consent from Premera is required to  
15 provide such access, Premera will grant such consent as is reasonably necessary to  
16 provide the Washington Foundation with such access.

17 *Duplicate Foundation Rights*

18 **Q. The state consultants in their supplemental reports assert that the two**  
19 **foundations should be entitled to certain rights which Premera did not**  
20 **include in its conversion filing. Please comment.**

21 A. Premera's original conversion filing proposed one foundation to receive 100% of  
22 the initial stock of New Premera at the time of conversion. It provided for a divestiture  
23 schedule under which the foundation would sell its New Premera shares down to less  
24 than 5% within a specified period of time. It further provided that 5% (less one share) of  
the foundation's stock would be voted freely by the foundation and not be subject to the  
Voting Trust Agreement which applies to the remainder of the foundation's stock. In

1 discussions with state consultants during October and December 2003, Premera was  
2 asked and agreed to give the foundation shareholder the right to designate a nominee to  
3 sit on the Premera Board of Directors.

4         In January 2004, the state consultants insisted that the transaction structure be  
5 changed to provide for two foundations, one for Washington and one for Alaska. The  
6 state consultants further asserted that, with the establishment of two foundations, (i) each  
7 foundation should be allowed to hold 5% (less one share) of the outstanding Premera  
8 stock free of all restrictions, (ii) each foundation should have a right to name a slate of  
9 candidates from which a "Designated Member" would be nominated to the Premera  
10 Board (or, in the alternative, in addition to a Washington Foundation Designated  
11 Member, the Alaska Health Foundation should be allowed to have an observer at the  
12 Premera Board), and (iii) each foundation should be subject to a separate, stand-alone  
13 divestiture schedule for its Premera shares (collectively the "Duplicate Foundation  
14 Rights"). Premera indicated to the state consultants that it would not object to these  
15 Duplicate Foundation Rights, provided such terms were approved by the BCBSA.  
16 Premera representatives immediately contacted BCBSA staff to confirm if the Duplicate  
17 Foundation Rights would be approved by BCBSA. BCBSA staff indicated that BCBSA  
18 would approve a waiver of the BCBSA license terms to permit the New Premera stock to  
19 be held by two separate foundations, one for Washington and one for Alaska, but  
20 reported that they would not recommend approval of two 5% (less one share) free voting  
21 blocks, two Designated Members (or one Designated Member and one observer), or  
22 separate divestiture schedules. Accordingly, Premera's February 5, 2004 conversion  
23 filing includes two foundations, as requested by the states, but does not include the  
24

1 Duplicate Foundation Rights. Mr. Barlow's pre-filed direct testimony discusses  
2 Premera's subsequent efforts to obtain BCBSA permission for the Duplicate Foundation  
3 Rights and the outcome of those efforts.

4 *Voting Trust Agreement*

5 **Q. On page 8 of the Blackstone Supplemental Report, related to the definition of**  
6 **"Change of Control" in the Voting Trust Agreement, Blackstone suggests**  
7 **that the shareholders pro forma ownership percentage threshold should**  
8 **change from 50.1% to 20.1%. Do you agree?**

9 A. No. The state consultants have consistently used the WellChoice transaction as  
10 their model of transaction structure "best practice." Our structure of 50.1% is precisely  
11 the WellChoice transaction term on this point. The BCBSA, which approved the 50.1%  
12 threshold in the WellChoice transaction, has advised Premera that it would not approve a  
13 reduction in the threshold. Maintaining the Blue marks is essential to the company and  
14 its members, is a prerequisite for this transaction, and Premera therefore cannot accede to  
15 the Blackstone recommendation on this point.

16 **Q. On page 8 of the Blackstone Supplemental Report, related to Section 3.02 of**  
17 **the Voting Trust Agreement, Blackstone suggests that the Washington**  
18 **Foundation should be allowed to maintain 5% of the outstanding common**  
19 **stock outside the trust at all times. How do you respond?**

20 A. The Washington Foundation is already afforded this right. The Form A  
21 Statement, as filed, provides that the Washington Foundation and the Alaska Health  
22 Foundation may each maintain 5% (less one share) of the outstanding common stock  
23 outside the Voting Trust with the following provisos: if the BCBSA does not approve of  
24 the Washington Foundation and the Alaska Health Foundation each holding 5% (less one  
share) outside the Voting Trust, and if the Washington Foundation and the Alaska Health  
Foundation cannot agree on a division of a single 5% (less one share) free voting block of

1 shares, then the Washington Foundation alone will hold 5% (less one share) outside the  
2 Voting Trust. Accordingly, the Washington Foundation will hold 5% (less one share)  
3 outside the Voting Trust unless it agrees otherwise. Premera would not be opposed to the  
4 Washington Foundation and the Alaska Health Foundation each holding 5% (less one  
5 share) of the outstanding common stock outside the voting trust if that were approved by  
6 BCBSA.

7 **Q. On page 8 of the Blackstone Supplemental Report, related to Section 3.02 of**  
8 **the Voting Trust Agreement, Blackstone expresses the view that the voting**  
9 **trust should cease to apply to the Washington Foundation when its**  
10 **ownership drops below 5% of the outstanding even if, in the aggregate, the**  
11 **Washington and Alaska foundations own more than 5%. How do you**  
12 **respond?**

13 A. Premera's filing is consistent with BCBSA instructions that a separate divestiture  
14 schedule would not receive BCBSA approval of an exception to BCBSA licensure  
15 requirements.

16 **Q. On page 8 of the Blackstone Supplemental Report related to Section 4.03(c)**  
17 **of the Voting Trust Agreement, Blackstone suggests that the Washington**  
18 **Foundation should be allowed to vote freely on any stock-based**  
19 **compensation programs that are in effect during the three years after the**  
20 **IPO. How do you respond?**

21 A. Premera intended for the Washington Foundation to vote freely on any stock-  
22 based compensation program put to a shareholder vote, other than the initial equity  
23 incentive plan (submitted with the Form A Statement), that would be in effect anytime  
24 during the three year period after the conversion and IPO. Premera acknowledges that  
the proviso included in Section 4.03(c) is confusing and does not reflect Premera's intent.  
Included is a technical correction in the form in Exhibit A attached hereto, if approved by  
the Commissioner and the BCBSA, should eliminate the concern stated by the state  
consultants.

1     **Q.     On page 8 of the Blackstone Supplemental Report related to Section 4.03(c)**  
2     **of the Voting Trust Agreement, Blackstone suggests that the Washington**  
3     **Foundation should be allowed to vote freely on any stock-based**  
4     **compensation programs that are effective after the three year Stock**  
5     **Restriction Period and submitted for a vote earlier than six months prior to**  
6     **the end of that period. How do you respond?**

7     A.     Premera's conversion filing provides that the Washington Foundation may freely  
8     vote on any stock-based compensation program that would become effective after the  
9     three year Stock Restriction Period and put to a shareholder vote during the first two  
10    years after the conversion and IPO. The state consultants state that such free voting  
11    should apply if the issue is put to a shareholder vote during the first two and one-half  
12    years after the conversion and IPO. Premera recognizes that the provisio in Section  
13    4.03(c) in the Voting Trust Agreement is confusing on this point as I noted above and  
14    believes the suggested technical correction addresses this. In addition, Premera is not  
15    opposed to this state consultants' suggestion that the Voting Trust Agreement should be  
16    modified to the effect that the Washington Foundation is able to freely vote on any stock-  
17    based compensation program that would become effective after the three year Stock  
18    Restriction Period and put to a shareholder vote during the first two and one-half years  
19    (rather than the two years in Section 4.03(c)) after the conversion and IPO, Premera  
20    would not object. This change, if approved by the Commissioner and the BCBSA,  
21    eliminate the concern stated by the state consultants.  
22  
23  
24

1 **Q. On page 9 of the Blackstone Supplemental Report related to Section**  
2 **5.03(b)(i) of the Voting Trust Agreement, Blackstone opines that Premera**  
3 **should be required to choose one of the three board nominees submitted by**  
4 **the Washington Foundation and should not have a right to veto nominees.**  
5 **How do you respond?**

6 A. The state consultants have consistently used the WellChoice transaction as their  
7 model of transaction structure “best practice.” The provision objected to by Blackstone is  
8 consistent with WellChoice.

9 The proposal to have a “Designated Member” on the Premera Board of Directors  
10 was accepted by Premera as an accommodation to a request by the state consultants,  
11 subject to Premera’s right to require additional nominees if the initial candidates were not  
12 accepted by the Premera Board. The state consultants did not object to that proviso at  
13 any time during the course of discussions prior to the filing of the Form A Statement  
14 amendments on February 5, 2004.

15 **Q. On page 9 of the Blackstone Supplemental Report, related to Section**  
16 **5.03(b)(ii) of the Voting Trust Agreement, Blackstone opines that the**  
17 **Washington Foundation’s right to designate a board member should not**  
18 **terminate after five years. How do you respond?**

19 A. The state consultants have consistently used the WellChoice transaction as their  
20 model of transaction structure “best practice.” In WellChoice the provision for a  
21 designated board member expires five years after the IPO or when the foundation owns  
22 less than 5% of the outstanding stock, whichever occurs earlier. The Premera proposal  
23 tracks WellChoice. In addition, we have been advised by the BCBSA that deviation from  
24 the WellChoice provision on the term of the designated board member would not be  
approved.

**Q. On page 9 of the Blackstone Supplemental Report, related to Section 7 of the**  
**Voting Trust Agreement, Blackstone opines that the divestiture requirements**

**for the first year should be eliminated as was done in the WellChoice conversion. How do you respond?**

A. I disagree. To meet BCBSA licensure requirements the Foundations must own less than 80% of the outstanding stock of Premera upon the completion of the IPO or within one year of the IPO. The WellChoice divestiture schedule did not explicitly require the Foundation to divest to 80% by the end of the first year because in WellChoice, more than 20% of the company was sold to the public at the IPO. Accordingly, there was no need for a first year 80% divestiture requirement.

**Q. On page 9 of the Blackstone Supplemental Report, related to Section 10 of the Voting Trust Agreement, Blackstone states that the Voting Trust Agreement should expire if Premera loses its Blue Cross Blue Shield license. How do you respond?**

A. We disagree. Such a provision would be wholly inappropriate. Blackstone's rationale is that the Voting Trust restrictions are due solely to the requirements of the BCBSA. Blackstone is mistaken. Even if there were no BCBSA requirements, the restrictions contained in the Voting Trust Agreement would be reasonable and necessary.

The Blackstone Supplemental Report points out that the Washington Foundation will be a large shareholder of a publicly traded entity and asserts that such status should give it certain rights and privileges. While it is true that the Washington Foundation will be a large shareholder, at least for a time, Blackstone fails to take into account important distinctions between the Washington Foundation and, for example, a large institutional investor as shareholders.

The purposes of the Washington Foundation differ greatly from those of a large institutional investor. The Washington Foundation's specific purposes are to promote the health of the residents of the State of Washington by undertaking certain actions which

1 are financed by the sale of the Premera stock received in the conversion. The  
2 Washington Foundation can only fund those actions and achieve its purposes by divesting  
3 itself of the Premera stock. In contrast, a large institutional investor invests its own  
4 money for the purpose of anticipated monetary gain, and is not obligated to sell its shares  
5 for any other reason than its own assessment of Premera as an investment.

6 Furthermore, termination of the Voting Trust Agreement as a result of the loss of  
7 the BCBSA license would be to the detriment to Premera's policyholders and the  
8 insurance buying public. Premera is currently managed under the direction of a board of  
9 directors with experience in providing oversight for a health carrier. If the Voting Trust  
10 were to terminate, decisions about Premera would be under the direction of a shareholder  
11 with no expertise in such matters. In fact, the interests of the Washington Foundation  
12 could be diametrically opposed to the interests of policyholders. The Washington  
13 Foundation's interest is to monetize the value of Premera rather than improving products  
14 and services for policyholders.

15 **Q. On page 21 of the Executive Summary of the C&B Supplemental Report,**  
16 **C&B state that New Premera should bear the full costs of the Trustee's**  
**expenses. How do you respond?**

17 A. The Premera transaction documents provide that there is an equal sharing of the  
18 Trustee's expenses between the Washington Foundation and Premera. This is fair and  
19 reasonable, and is in line with the WellChoice transaction, which is cited by the state  
20 consultants as "best practice." As C&B points out, such equal sharing of expenses is a  
21 fair proposition as compared to precedent transactions.

22 C&B wants to deviate from WellChoice by asking that Premera alone bear the  
23 Trustee costs. C&B asserts that Premera is imposing "unnecessary" conditions. I am not  
24

1 aware of any unnecessary conditions, and C&B does not articulate what they might be.  
2 There is no support for the proposition that the equal sharing of Trustee expenses  
3 between the Washington Foundation and Premera is unfair.

4 Registration Rights Agreement

5 **Q. On page 10 of the Blackstone Supplemental Report, related to Section 3(f) of**  
6 **the Registration Rights Agreement, Blackstone suggests that the Washington**  
7 **Foundation should be permitted, to the fullest extent possible, to continue a**  
8 **registration by Premera from which Premera has decided to withdraw. How**  
9 **do you respond?**

10 A. Blackstone misinterprets the agreement. The Washington Foundation has the  
11 rights that Blackstone seeks in this regard. All the foundation must do to exercise those  
12 rights is ask. It is the Company that registers the securities and it is the Company's  
13 registration statement, so technically the Foundation can't continue the registration if the  
14 Company decides not to file, or decides to withdraw, a registration where the Company  
15 has given notice to the Foundation of Piggy-Back rights. Notwithstanding this technical  
16 point, the Company gave the Foundation the practical rights it was seeking. Specifically,  
17 Section 3(f) of the Registration Rights Agreement provides that in the event the Company

18 ". . . should decide to withdraw such a registration, the Company shall  
19 give the Foundations advance notice at least three (3) business days prior  
20 to any proposed non-filing or withdrawal pursuant to the preceding  
21 sentence, and shall, if requested by the Piggy-Back Foundation and to the  
22 extent practicable, endeavor to maintain such Registration Statement on  
23 file and effective in such a manner so as to allow the Piggy-Back  
24 Foundation to exercise its Piggy-Back Rights, and in any event, the  
Foundations shall thereafter have the right to provide notice of a Demand  
Registration pursuant to Section 2 [of the Registration Rights  
Agreement]."

1 **Q. On page 10 of the Blackstone Supplemental Report, related to Section 9 of**  
2 **the Registration Rights Agreement, Blackstone suggests that the Washington**  
3 **Foundation should have input in the pricing decision in the event of a**  
4 **Washington Foundation Demand where Premera piggybacks. How do you**  
5 **respond?**

6 A. The Registration Rights Agreement already provides the Washington Foundation  
7 with the input in the pricing decision Blackstone seeks. The Washington Foundation, in  
8 connection with any underwritten offering made pursuant to its own demand, or if joined  
9 by the Alaska Health Foundation where the Washington Foundation is offering a larger  
10 number of shares than Alaska, will select a joint bookrunning managing underwriter to  
11 manage the underwritten offering and act as the stabilization agent. The input Blackstone  
12 seeks will be provided by such joint bookrunning managing underwriter, who will  
13 certainly be working with the pricing committee for the offering.

14 Premera's Bylaws

15 **Q. On page 10 of the Blackstone Supplemental Report, related to Article II,**  
16 **Section 4, of the Registration Rights Agreement, Blackstone suggests that the**  
17 **definition of "Independence" for Premera's board of directors needs to be**  
18 **adjusted by lowering the 2% of revenue test. How do you respond?**

19 A. As defined in Premera's Bylaws, a director is independent if the director is not  
20 currently an employee or executive officer of another company that accounts for at least  
21 two percent or \$1 million, whichever is greater, of New Premera's consolidated gross  
22 revenues. This definition mirrors that found in the similar provision of the New York  
23 Stock Exchange ("NYSE") "Listed Company Manual." That manual, and specifically  
24 that provision, were recently amended to implement significant changes to the NYSE's  
listing standards that are aimed to ensure the independence of directors of listed  
companies and to strengthen corporate governance practices of listed companies. The  
amendments were approved by the Securities and Exchange Commission ("SEC") in late

2003. In the SEC's view, the amended NYSE rules will foster greater transparency, accountability and objectivity in the oversight by, and decision-making processes of, the boards and key committees of NYSE-listed companies.

There is no logic for requiring New Premera to have a definition of an independent director which is more restrictive than the NYSE rules, especially given the approval of the rules by the SEC. Blackstone suggestion that New Premera should operate in a manner required of no other NYSE-listed company is arbitrary.

*Unallocated Share Escrow Agent Agreement*

**Q. Blackstone, on page 11 of the Blackstone Supplemental Report, comments on the Unallocated Share Escrow Agent Agreement. Have you read Blackstone's comments? If so, do you have any reaction?**

A. Yes, I have read the Blackstone comments regarding the Unallocated Share Escrow Agent Agreement. Please see the Supplemental Report of John M. Steel for a full discussion of why such an agreement is required, as well as the Supplemental Report of Banc of America Securities, which states that the implementation of such an agreement will not have a negative effect on Premera's market value. I will limit my comments regarding the Unallocated Share Escrow Agent Agreement to the following.

The Unallocated Share Escrow Agent Agreement becomes effective only if Washington and Alaska are unable to agree upon the allocation of Premera's stock between the two foundations. The two states have been working on this issue for well over a year and have yet to agree on an allocation of the stock. The OIC and Alaska Department of Insurance have not brought the allocation discussions to closure and there is no assurance they will do so by the time of the hearing, the Commissioner's decision,

1 or even the closing date of the conversion itself. The Unallocated Share Escrow  
2 Agreement is therefore necessary to address that possibility.

3 The C&B Supplemental report states that Premera's failure to specify an  
4 allocation of the shares in New Premera between the two foundations is "a fatal defect in  
5 the application." That statement is directly inconsistent with the facts. The state  
6 consultants have insisted that the two states would determine the allocation of New  
7 Premera's shares. We have been repeatedly told this is to be resolved solely by the states  
8 without participation by Premera.

9 *Articles of Incorporation and Bylaws of the Washington Foundation*

10 **Q. The C&B Supplemental Report on Page 2, footnote 2, points out that**  
11 **Premera referred to the Foundation to be established in the State of**  
12 **Washington as the "Washington Foundation Shareholder" rather than the**  
13 **"Washington Foundation". How do you respond?**

14 A. Premera does not object to using the term "Washington Foundation" in place of  
15 "Washington Foundation Shareholder" in the Form A filing. In any event, the name  
16 "Washington Foundation" would be merely a placeholder in the transaction documents  
17 until the final proper name for the charitable entity can be established. The name  
18 "Washington Foundation," suggested by C & B, is not available in the State of  
19 Washington and thus it would be inappropriate to name the entity as such.

20 **Q. The Executive Summary of the C&B Supplemental Report states on page 14,**  
21 **"PREMERA has excluded from the Washington Foundation's Board of**  
22 **Directors those individuals who are members of 'any hospital or hospital**  
23 **association or medical association in Washington.'" Is this an accurate**  
24 **statement? If not, please comment.**

25 A. No. The C&B Supplemental Report as quoted above suggests physicians would  
26 be excluded from the Washington Foundation board. That is simply inaccurate.  
27 Premera's Form A Statement expressly contemplates that physicians can be on the

1 Washington Foundation board. Exhibit E-2 to the Form A Statement excludes persons  
2 who are directors, officers or employees of a hospital, hospital association or medical  
3 association in Washington. There is no blanket exclusion of all physicians who are  
4 members of a medical association.

5 **Q. On page 15 of the Executive Summary of the C&B Supplemental Report,**  
6 **C&B states that Article IX and Article X of the Articles of Incorporation of**  
7 **the Washington Foundation Shareholder contain a prohibition upon**  
8 **amending, altering or repealing the Articles of Incorporation or Bylaws, and**  
9 **that such a prohibition will impede the Foundation's ability to satisfy IRS**  
10 **concerns regarding the Foundations tax status. How do you respond?**

11 A. C&B is mistaken in its reading of the Articles of Incorporation. No such  
12 prohibition exists. Article IX as to the Bylaws provides:

13 Bylaws of the Corporation may be adopted by the Board of  
14 Directors at any regular meeting or any special meeting called for  
15 that purpose, so long as they are not inconsistent with the  
16 provisions of these Articles of Incorporation. The authority to  
17 make, alter, amend, or repeal Bylaws is vested in the Board of  
18 Directors and may be exercised at any regular or special meeting  
19 of the Board of Directors by the affirmative vote of three-fourths  
20 (3/4) of the directors then in office and advance written approval of  
21 the Attorney General of the State of Washington.

22 Further, Article X as to the Articles provides:

23 These Articles of Incorporation may be amended by the  
24 directors upon (i) the affirmative vote of three-fourths (3/4) of the  
directors then in office, but in no event can Article III ("Purposes  
and Powers") be amended to be inconsistent with the purpose of  
promoting the health of the residents of the State of Washington;  
and (ii) other than with respect to amendments of Article XI  
("Registered Office and Agent"), no amendments to the Articles of  
Incorporation may be adopted without the advance written  
approval of the Attorney General of the State of Washington.

Clearly the Washington Foundation can amend both its Articles of Incorporation  
and Bylaws. If the Washington Foundation needs to amend either its Articles of

1 Incorporation or Bylaws to satisfy IRS concerns to achieve § 501(c)(4) status, obtaining  
2 the required three-fourths vote and Attorney General approval should not be an obstacle.

3 **Q. On page 19 of the Executive Summary of the C&B Supplemental Report,**  
4 **related to the Articles of Incorporation of the Washington Foundation**  
5 **Shareholder and the Bylaws of the Washington Foundation Shareholder,**  
6 **C&B asserts that the appointment of the Investment Committee at the time**  
7 **the initial Board of Directors (the “First Board”) is installed may raise an**  
8 **issue of independence. How do you respond?**

9 A. The appointment of the Investment Committee by the First Board does not create  
10 an independence issue. The First Board will be appointed solely to create the Foundation  
11 and to apply to the Internal Revenue Service for recognition of the organization's tax-  
12 exempt status. It will not have any Investment Committee functions as the Washington  
13 Foundation will not hold any Premera stock until after the state approvals have been  
14 obtained and the conversion and IPO has occurred. Once all state and regulatory  
15 approvals of the State of Washington have been obtained and the Second Board has been  
16 appointed by the Attorney General of the State of Washington, the First Board will resign  
17 and take all actions necessary to effect the installation of the Second Board. The Second  
18 Board, upon appointment by the Attorney General, will be in place for a period  
19 commencing soon after the approval of the conversion and through the IPO which would  
20 avoid any independence issue.

21 *Duration of Economic Assurances*

22 **Q. In the PwC Economic Consultants’ Supplemental Report, PwC recommends**  
23 **that the term of the Washington Economic Assurances in the Form A**  
24 **Statement be lengthened from two years to three or more years. Do you**  
25 **agree with PwC’s recommendation?**

26 A. No. PwC “believes” that Premera’s assurances must be extended to three years or  
27 longer to provide an “appropriate” level of protection. PwC, however, does not define

1 what it means by appropriate or give any evidence or support for the proposition that two  
2 years is inappropriate. On the other hand, Banc of America Securities, National  
3 Economic Research Associates, and Milliman USA explain why a term longer than two  
4 years for the Washington Economic Assurances would be inappropriate. I agree with  
5 these experts' opinions.

6 Banc of America Securities' Supplemental Report speaks to the Washington  
7 Economic Assurances and states: "With respect to these types of assurances, investors  
8 will want certainty that those economic assurances do not negatively impact the company  
9 from a financial or competitive standpoint." A longer timeframe increases the risk that  
10 the assurances would impair Premera's ability to achieve its financial projections or  
11 would place the company at a competitive disadvantage.

12 National Economic Research Associates ("NERA") in its Supplemental Report  
13 concurs: "the assurances will likely create operational inflexibilities and potential  
14 competitive disadvantages for Premera that can only worsen over time." The  
15 Washington market is competitive. NERA provides examples how Premera's  
16 competitors can leverage the assurances to Premera's detriment.

17 Milliman USA states in its Supplemental Report: "Because changes in the  
18 marketplace are difficult to predict, it would be an unsound business practice for a  
19 company such as Premera to make such a rate-related assurance that extends beyond a  
20 one to two year period, particularly if competitors are not bound by similar assurances."  
21 Premera's competitors will not be bound by similar assurances. The longer the term of  
22 the assurances, the greater the probability that the assurances will put Premera at a  
23 competitive disadvantage.  
24

**Q. Do you have any other comments regarding the Form A Statement?**

A. Yes. We have identified a number of drafting items in the Form A filing, such as typographical errors or text which the state consultants felt was ambiguous or did not reflect the intent. Corrections for those items are attached hereto as Exhibit A, and will be marked as a Premera Hearing Exhibit.

**Q. Does that conclude your direct testimony?**

A. Yes, it does.



## SUMMARY OF TECHNICAL DRAFTING CORRECTIONS TO PROPOSED PREMERA CONVERSION DOCUMENTS

The corrections described below do not represent substantive changes in the Form A documents. They make corrections such as typographical errors or text which the state consultants felt was ambiguous or did not reflect the intent. Capitalized terms used but not otherwise defined herein have the meanings set forth in the relevant document. All page references are to the clean versions of the documents that are attached to Change No. 1 to the Statement Regarding the Acquisition of Control of a Domestic Health Carrier and a Domestic Health Insurer, filed with the Insurance Commissioner of the State of Washington, the Alaska Division of Insurance, and the Oregon Insurance Division by [New PREMERA Corp.] on February 5, 2002 (the "Amended Form A").

### Articles of Amendment of the Articles of Incorporation of PREMERA (the "PREMERA Articles of Amendment"), Exhibit A-2 to the Amended Form A:

- Article XII of the Articles of Amendment: Dissolution, Section 2 (page 2) – This makes clear that the Foundations may amend their Articles of Incorporation and Bylaws to meet IRS requirements for recognition as organizations exempt from federal taxation under Section 501(a) of the Internal Revenue Code. Permitting amendment of the Articles of Incorporation and the Bylaws for such purposes is implicit in the Foundations' Articles of Incorporation (Exhibits E-1 and E-3). Because the applications for tax-exempt status may still be pending when the Commissioner issues his decision, such flexibility should be made explicit in the PREMERA Articles of Amendment.
- Article XII of the Restated Articles of Incorporation of PREMERA: Dissolution, Section 2 (page 8) – This is the same correction as in the PREMERA Articles of Amendment, discussed above.

### Plan of Conversion (the "Plan"), Exhibit A-4 to the Amended Form A:

- Article I, Definition of "Access" (page 2) – This is a technical correction that clarifies the requirement of presentation to advisors for the states of Washington and Alaska by specifying that the presentation must occur at least thirty days prior to the Public Offering road show.
- Section 4.3(a)(vii) (page 8) – This is a technical correction to include specific references to the Guaranty Agreement and to Common Stock and Class B Common Stock in place of the general references.
- Section 4.3(b)(i) (page 12) – This is a typographical correction to delete the reference to subsection 4.3(a)(xv). This clarifies the intent that the approval specified in subsection 4.3(a)(xv) is a condition to closing but that the receipt of approval is not required to begin

the period during which the closing of the Conversion shall occur, as described in Section 4.3(b) of the Plan.

- Section 4.3 (b)(ii)(D) and (E) (page 12) – These corrections are designed to remove possible ambiguities and to clarify the appropriate measurements for the Reportable Changes.
- Section 5.3(a) (page 13) – This technical correction makes explicit what the parties anticipate, namely that the Conversion is effective upon “closing” of the Public Offering (i.e., payment for and transfer of the Common Stock in the Public Offering).
- Exhibit G, Transaction Steps (page 3) – These are technical drafting corrections to refer to the Common Stock and Class B Common Stock of New PREMERA, specifically to reflect the delivery of the Class B Common Stock to the Washington Foundation. A correction is also made in Step 19 to reflect that PREMERA will contribute its New PREMERA stock to the Foundations, not to PREMERA.

Articles of Incorporation of New PREMERA (the “Articles of Incorporation”), Exhibit B-1 to the Amended Form A:

- Article III, Section 5(b)(2) (page 9) – This is a minor drafting correction defining “Nominating Shareholder.” The term was previously used but not explicitly defined.

Bylaws of New Premera Corp. (the “Bylaws”), Exhibit B-2 to the Amended Form A:

- Article II, Section 4 (page 5) – This is a technical correction making explicit that the qualifications for New PREMERA’s Board of Directors encompass the “independence” requirements set forth in Article II, Section 4 of the Bylaws (mandated by the New York Stock Exchange listing standards), as well as those set forth in Article III, Section 4 of the Articles of Incorporation (mandated by the Blue Cross Blue Shield Association). This was previously implicit when the Articles of Incorporation and the Bylaws were read together.
- Article III, Section 6(b)(1) (page 10) – This is a minor drafting correction prohibiting employees of Subsidiaries of New PREMERA from serving on the Nominating and Governance Committee, just as they are prohibited from serving on the Audit Committee. This was implicit in Article III, Section 1 regarding committee compliance with listing requirements.

Transfer, Grant and Loan Agreement (the “TGLA”), Exhibit G-3 to the Amended Form A:

- Fifth WHEREAS clause (page 1) – These technical drafting corrections reflect specifically the Common Stock and Class B Common Stock.

- Section 1.01 (page 2) – This corrects an inconsistency between Section 1.02 and Sections 1.02.1 and 1.02.2 and clarifies the intent of the provisions, taken together. The reference in Section 1.02 should be to Section 501(a) of the Internal Revenue Code (rather than Section 501(c)(3)), as provided in Sections 1.02.1 and 1.02.2.
- Section 3.02 (page 5 and 6) – These corrections are also necessary as part of the correction of the inconsistent provisions noted above. Section 3.02 should also refer to Section 501(a) of the Internal Revenue Code.
- Article IV (page 7) – This correction specifies that the representations and warranties will be made as of the Closing Date. This removes an unintentional ambiguity.

Voting Trust and Divestiture Agreements (the “VTDA”), Exhibit G-4 to the Amended Form A:

- Section 4.03(c) (pages 11-12) – This clarifies a confusing proviso in Section 4.03(c), which did not reflect Premera’s intent. Shares of New PREMERA Common Stock held in the Voting Trust will be voted as directed by the Beneficiaries (i.e., the Foundations) on any new Stock-Based Program that is effective during the Stock Restriction Period and on any new Stock-Based Program that is effective after the Stock Restriction Period but submitted to a shareholder vote for approval prior to the last twelve months of the Stock Restriction Period. The reference to Section 4.03(d) is changed to Section 4.03(e) to reflect the split in Section 4.03(d) as part of this clarification.
- Section 4.03(d) and (e) (page 12) – These corrections split Section 4.03 (d) into two sections to address the issue with the proviso in Section 4.03(d) and clarify the intent as noted above. Section 4.03(e) has been renumbered to subsection (f) to reflect the split in Section 4.03(d).
- Section 7.04 (page 17 in original and page 18 in corrected version) – This is a minor drafting correction clarifying that the Class B Common stock will automatically convert when the Beneficiary owns less than five percent of the Capital Stock of New PREMERA, as set forth in Article II, Section 2(f) of the New PREMERA Articles of Incorporation.

**Articles of Amendment of the Articles of Incorporation of PREMERA  
Exhibit A-2 to the Amended Form A**

4. Article VII shall be deleted in its entirety and shall be replaced with the following:

**Article VII: Members**

The voting members of the Corporation shall be [Washington Foundation Shareholder], a Washington nonprofit corporation, and [Alaska Health Foundation], an Alaska nonprofit corporation. Whenever the term "voting members," "voting membership" or "Foundations" appear in these Articles of Incorporation, they shall be deemed to refer to [Washington Foundation Shareholder] and [Alaska Health Foundation].

5. Article XII shall be amended to read as follows:

**Article XII: Dissolution**

Section 1. Recipient of Distribution of Assets and Permissible Purposes. Upon the winding up and dissolution of the Corporation, the assets of the Corporation remaining after payment of, or provision for payment of, all debts and liabilities of the Corporation (the "Liquidation Proceeds"), shall be distributed in the manner and solely for the purposes set out below:

A. If the Foundations fulfill the conditions set forth in Section 2 of this Article XII, the Liquidation Proceeds shall be distributed to the Foundations, subject to the limitations set forth in this Article XII, to be used exclusively to promote the health of the residents of the States of Washington and Alaska.

B. If the voting members do not fulfill the conditions set forth in Section 2 of this Article XII, the Liquidation Proceeds shall be distributed, subject to the limitations set forth in this Article XII and approval of the Washington and Alaska Attorneys General, to one or more nonprofit corporations or other nonprofit entities upon the adoption of a resolution of the Board of Directors stating the amount of each distribution and identifying each nonprofit corporation or other nonprofit entity, to be used exclusively to promote the health of the residents of the states of Washington and Alaska.

C. Any distribution of the Liquidation Proceeds shall be subject to the limitations of applicable law, including federal tax law and any contractual obligations associated with the Foundations' receipt of such proceeds.

Section 2. Conditions for Distribution. The Liquidation Proceeds shall be distributed to each of the Foundations only if ~~the Foundations~~such Foundation (a) ~~have~~has been recognized or ~~have~~has applied for recognition by the Internal Revenue Service as exempt from federal taxation under Section 501(a) of the Internal Revenue Code of 1986, as amended; and (b) ~~have~~has not (i) amended, altered or repealed ~~their respective~~its Articles of Incorporation; or (ii) amended, altered or repealed ~~their respective Bylaws or its Bylaws,~~ other than as may be required by the Internal Revenue Service for recognition of such Foundation as exempt from federal taxation under Section 501(a) of the Internal Revenue Code.

Section 6. Repeal or Modification. No repeal or modification of this Article X shall adversely affect any right or protection of any such director, officer, employee, physician consultant, or member of a committee or panel of the Corporation, including, but not limited to, a medical advisory committee or panel, existing at the time of such repeal or modification for or with respect to any act or omission of such person occurring prior to such repeal or modification.

## **Article XI: Bylaws**

The authority to alter, amend or repeal bylaws is vested in the Board of Directors and shall be exercised as provided in the Bylaws.

## **Article XII: Dissolution**

Section 1. Recipient of Distribution of Assets and Permissible Purposes. Upon the winding up and dissolution of the Corporation, the assets of the Corporation remaining after payment of, or provision for payment of, all debts and liabilities of the Corporation (the "Liquidation Proceeds"), shall be distributed in the manner and solely for the purposes set out below:

A. If the Foundations fulfill the conditions set forth in Section 2 of this Article XII, the Liquidation Proceeds shall be distributed to the Foundations, subject to the limitations set forth in this Article XII, to be used exclusively to promote the health of the residents of the States of Washington and Alaska.

B. If the voting members do not fulfill the conditions set forth in Section 2 of this Article XII, the Liquidation Proceeds shall be distributed, subject to the limitations set forth in this Article XII and approval of the Washington and Alaska Attorneys General, to one or more nonprofit corporations or other nonprofit entities upon the adoption of a resolution of the Board of Directors stating the amount of each distribution and identifying each nonprofit corporation or other nonprofit entity, to be used exclusively to promote the health of the residents of the states of Washington and Alaska.

C. Any distribution of the Liquidation Proceeds shall be subject to the limitations of applicable law, including federal tax law and any contractual obligations associated with the Foundations' receipt of such proceeds.

Section 2. Conditions for Distribution. The Liquidation Proceeds shall be distributed to each of the Foundations only if the Foundation ~~such Foundation~~ (a) ~~have~~has been recognized or ~~have~~has applied for recognition by the Internal Revenue Service as exempt from federal taxation under Section 501(a) of the Internal Revenue Code of 1986, as amended; and (b) ~~have~~has not (i) amended, altered or repealed their respective its Articles of Incorporation; ~~or (ii) amended, altered or repealed their respective Bylaws.~~ or its Bylaws, other than as may be required by the Internal Revenue Service for recognition of such Foundation as exempt from federal taxation under Section 501(a) of the Internal Revenue Code.

**Plan of Conversion,  
Exhibit A-4 to the Amended Form A**

After the completion of the Conversion, the Washington Foundation Shareholder and Alaska Health Foundation will collectively own 100% of the capital stock of New PREMERA, and New PREMERA will directly control PBC-AK and New PBC and indirectly control all of New PBC's subsidiaries including LifeWise Assurance Company, a Washington for-profit insurance company ("LWA"), New LifeWise Washington Corp., LifeWise Health Plan of Arizona, Inc., a Washington for-profit insurance company ("LW-AZ"), and LifeWise Health Plan of Oregon, Inc., an Oregon for-profit insurance company ("LifeWise Oregon," and together with LWA, New LifeWise Washington, and LW-AZ, collectively, the "Subsidiaries"). The Washington Foundation Shareholder and Alaska Health Foundation will gradually divest themselves of the shares of New PREMERA stock over a period of time. The Washington Foundation Shareholder shall use the resultant net proceeds to promote the health of the residents of the State of Washington and Alaska Health Foundation shall use the resultant net proceeds to promote the health of the residents of the State of Alaska.

Capitalized terms used but not defined herein shall have the respective meanings set forth in the Form A (as defined below).

## ARTICLE I

### DEFINITIONS

As used in this Plan of Conversion, the following capitalized terms have the following meanings (if capitalized terms are not defined herein, such terms have the meaning given in the Form A):

"Access" shall mean (A) all reasonable access to (i) the drafts of the S-1 Registration Statement for the Public Offering for purposes of reviews and comments and filing the same with the Securities and Exchange Commission ("SEC"), (ii) drafts of response letters to the SEC comments (including materials supplementally provided to the SEC), (iii) the preparation and conducting of the Public Offering roadshow, including, but not limited to, (a) any presentation to New PREMERA by its financial advisors related to the contemplated size of the IPO, the split between primary and secondary shares, and the pricing range of the Common Stock prior to the roadshow, (b) a presentation to the advisors of the states of Washington and Alaska on the foregoing issues to occur no later than thirty (30) days prior to the commencement of the roadshow, and (c) attendance at selected meetings and presentations during the roadshow, and (iv) the processes of book-building for and pricing the Public Offering, and (B) the receipt and review of, and the opportunity to comment on, draft and final copies of such Public Offering-related documents and materials, including, without limitation, (i) SEC filings and responses to SEC comments, (ii) the underwriting agreement, (iii) roadshow slides and Internet pages, (iv) information and materials prepared by the Company's lead underwriters relevant to pricing and size of the offering, and (v) other investor presentation materials, in each case substantially contemporaneous with the distribution thereof to the investment banking firm or firms acting as New PREMERA's financial advisor in connection with the Public Offering and/or as bookrunning lead managing underwriter for the Public Offering.

"Alaska Health Foundation" has the meaning set forth in the Preamble hereof.

(B) the Board of Directors of the Washington Foundation Shareholder shall have approved and authorized the execution, delivery and performance by the Washington Foundation Shareholder of the Transfer, Grant and Loan Agreement, the License Agreement, the Voting Trust Agreement (to which it is a party), the Registration Agreement and any other Plan of Conversion Document to which the Washington Foundation Shareholder is a party, and

(C) the Washington Foundation Shareholder shall have received (or applied for) a determination letter from the Internal Revenue Service that it is exempt from taxation under Section 501(a) of the Code.

(v) *Alaska Health Foundation.* With regard to the Alaska Health Foundation:

(A) the Alaska Health Foundation shall be duly organized, validly existing and in good standing as a non-profit corporation under the laws of the State of Alaska and shall be operating under the Alaska Health Foundation Articles of Incorporation and Bylaws,

(B) the Board of Directors of the Alaska Health Foundation shall have approved and authorized the execution, delivery and performance by the Alaska Health Foundation of the Transfer, Grant and Loan Agreement, the License Agreement, the Voting Trust Agreement (to which it is a party), the Registration Agreement and any other Plan of Conversion Document to which Alaska Health Foundation is a party, and

(C) the Alaska Health Foundation shall have received (or applied for) a determination letter from the Internal Revenue Service that it is exempt from taxation under Section 501(a) of the Code.

(vi) *PBC.* The Board of Directors of PBC shall have approved and authorized the transfer of certain of its assets and liabilities directly related to its operations in Alaska to PBC-AK in exchange for 100% of the stock of PBC-AK pursuant to the Alaska Transfer Agreement, the transfer of its other assets and liabilities, including its health care service contractor registration in the State of Washington (and including the stock of PBC-AK) to New PBC in exchange for 100% of the stock of New PBC, the liquidation of PBC and distribution of its New PBC stock to PREMERA pursuant to the PBC Transfer Agreement, and the consummation by PBC of the other transactions as contemplated herein.

(vii) *PREMERA.* The Board of Directors of PREMERA shall have approved and authorized the execution, delivery and performance by PREMERA of the Transfer, Grant and Loan Agreement, the Guaranty Agreement and any other Plan of Conversion Document to which PREMERA is a party, the transfer of its assets and liabilities to New PREMERA in exchange for 100% of the ~~stock~~ Common Stock and Class B Common Stock of New PREMERA, and the liquidation of PREMERA and distribution of its ~~remaining asset, the New PREMERA stock,~~ Common Stock and Class B Common Stock to the Washington Foundation Shareholder and New PREMERA Common Stock to the

imposition of the Washington sales, use, business and occupation, or real estate transfer taxes to the transfers of assets pursuant to the Plan of Conversion, which would result in a material tax amount to the parties to the Plan of Conversion.

(b) Closing of Conversion. (i) The closing of the Conversion shall occur on a date to be determined by PREMERA upon fulfillment or waiver of all of the conditions specified in Section 4.3(a) (the "Closing Date"), which shall be in no event later than twelve (12) months following the receipt of all of the approvals set forth in subsections (a)(i)-(a)(iii), (a)(xiv), ~~(a)(xv)~~ and (a)(xvii) of this Section 4.3. Notwithstanding the foregoing, in the event there is any pending litigation related to the Conversion on the Closing Date, the 12-month period set forth above shall be extended by up to two successive three (3) month periods and, in addition, any approval period may be extended at the discretion of the Washington Insurance Commissioner and the Alaska Division of Insurance.

(ii) In order to assist the external consultants retained by the Washington Insurance Commissioner and the Alaska Division of Insurance in preparing bring down opinions in support of their respective reports to the Washington Insurance Commissioner and the Alaska Division of Insurance regarding the Conversion, PREMERA shall certify, pursuant to the form of certificate set forth on Exhibit H hereto, whether any Reportable Change has occurred, and if so, shall specify the nature of any such Reportable Change that has occurred (the "Reportable Change Certification"), in each case, from October 1, 2003, through the Closing Date. PREMERA shall provide the proposed Reportable Change Certification at least thirty (30) days but no more than sixty (60) days prior to the Closing Date, and the certification shall be effective as of the Closing Date. For purposes of this Section 4.3(b), a "Reportable Change" shall mean (A) any material change in the forms of documents appearing as exhibits to the Form A, (B) any material change in PREMERA's current elections or filing positions for federal or state income tax purposes from those reflected in PREMERA's tax returns for 2002, or any imposition of the Washington sales, use, business and occupation, or real estate transfer taxes to the transfers of assets pursuant to the Plan of Conversion that would result in a material tax amount to the parties to the Plan of Conversion, (C) any material change in PREMERA's ability to meet the assurances made by PREMERA to the Washington Insurance Commissioner or the Alaska Division of Insurance, as the case may be, as set forth in Exhibit E-8 herein, (D) (x) for PREMERA on a consolidated basis and for Alaska separately, any decrease in underwriting margin or operating margin, in excess of two (2) percentage points as compared to the companies' projections dated March 21, 2003 or (y) with respect to the combined operations of PREMERA in Alaska and Washington, any decrease in enrollment of more than ten percent (10%) by any insured line of business (individual, small group, large group or FEP, but excluding Healthy Options/BHP) or decrease in total enrollment of more than five percent (5%) ~~compared to actual enrollment, such change as to be determined by based upon the annual quarterly statutory statements~~ statement ~~filed by health plans with the Washington Insurance Commissioner or the Alaska Division of Insurance prior to the Closing Date;~~ (E) any change in PBC's or its affiliates' ~~prior-affiliated~~ ratings, any new rating, or the announcement of the placing of any such rating on "watch list", "under review" or "on surveillance" status from A.M. Best, Standard and Poor's Corporation, or any other nationally recognized statistical rating organization with which PBC or its affiliates have contracted, (F) a change of more than fifty (50) percentage points in PBC's Risk-Based Capital position based upon PBC's Risk-Based

Capital report filed with the Washington Insurance Commissioner or the Alaska Division of Insurance for the year ending December 31, 2003 compared to PBC's most recent Risk-Based Capital report on file with the Washington Insurance Commissioner or the Alaska Division of Insurance prior to the Closing Date, (G) any material change in the recommendation of PREMERA's investment banking or financial consultants relating to the Conversion or any recommendations from such new consultants that contradict the previous investment banking or financial consultant recommendations regarding the Conversion, or (H) any new lawsuits or any material adverse change in the accrued liabilities for any lawsuit against PREMERA.

(c) Exhibit G hereto sets forth the transaction steps to be taken to effect the Conversion on or in connection with the Closing Date.

## ARTICLE V

### ADDITIONAL PROVISIONS

5.1 Amendments. PREMERA may amend, restate and supplement this Plan of Conversion, and upon doing so, will promptly provide copies thereof to the Washington Insurance Commissioner, the Attorney General of the State of Washington, the Alaska Division of Insurance and the Oregon Insurance Division.

5.2 Cancellation. PREMERA, PBC and LifeWise Washington are not obligated to proceed with a Conversion. PREMERA, PBC and LifeWise Washington are concerned that any action approving the Form A by the Washington Insurance Commissioner, the Attorney General of the State of Washington, the Alaska Division of Insurance and the Oregon Insurance Division could contain conditions that might not be acceptable to PREMERA and PBC. Therefore, PREMERA, PBC and LifeWise Washington expressly reserve the right, at any time prior to the closing of the Conversion, to cancel and abandon this Plan of Conversion, and upon doing so, will promptly provide notice thereof to the Washington Insurance Commissioner, the Attorney General of the State of Washington, the Alaska Division of Insurance and the Oregon Insurance Division.

5.3 Public Sale of Common Stock. (a) On the Closing Date, New PREMERA and/or the Foundation Shareholder will offer and sell to the public shares of Common Stock (the "Public Offering"), subject to the terms of the Voting Trust and Divestiture Agreements and Registration Rights Agreement, as applicable. It shall be a condition subsequent to the effectiveness of the Conversion that the Public Offering be settled and closed, such that shares of Common Stock are exchanged with the Public Offering purchasers for cash, within three business days of the Closing Date.

(b) New PREMERA will select as managing underwriters for the Public Offering investment banking firm or firms of national reputation. The managing underwriters will conduct the Public Offering in a manner generally consistent with customary practices for initial public offerings of a type, size and nature comparable to the Public Offering. An investment banking firm acting on behalf of the Washington Insurance Commissioner and an investment banking firm acting on behalf of the Alaska Division of Insurance (each an "IPO Advisor" and

- Step 17. New PREMERA shall issue to PREMERA 100% of its outstanding capital stock and shall issue a stock certificate to PREMERA evidencing such shares of Common Stock and Class B Common Stock in exchange for all of the assets and liabilities of PREMERA.
- Step 18. PREMERA, New PREMERA, the Washington Foundation Shareholder, and Alaska Health Foundation shall execute and deliver to each other the Transfer, Grant and Loan Agreement.
- Step 19. PREMERA shall perform a statutory liquidation and contribute its remaining asset, the New PREMERA stock, ~~to PREMERA~~ as follows: the Common Stock to the Washington Foundation Shareholder and the Alaska Health Foundation, and the Class B Common Stock to the Washington Foundation Shareholder. Such contribution shall be evidenced by PREMERA's endorsement for transfer and delivery to the Washington Foundation Shareholder and Alaska Health Foundation of the New PREMERA stock certificate delivered to PREMERA pursuant to Step 17 above.
- Step 20. The Board of Directors of the Washington Foundation Shareholder and the Alaska Health Foundation shall approve and authorize the execution of the Registration Rights Agreement. The Washington Foundation Shareholder and the Alaska Foundation shall approve and authorize the execution of the Registration Rights Agreement.
- Step 21. The Washington Foundation Shareholder, Alaska Health Foundation, and New PREMERA shall execute and deliver to each other the Registration Rights Agreement.
- Step 22. To comply with requirements imposed by the BCBSA, the Washington Foundation Shareholder, Alaska Health Foundation, New PREMERA and the Trustee designated therein shall execute and deliver to the others the applicable Voting Trust Agreements, and certificates evidencing shares of the New PREMERA stock required to be deposited in trust pursuant to the terms of such Agreements shall be endorsed and delivered by the Washington Foundation Shareholder and Alaska Health Foundation to the Trustee.
- Step 23. In the event there is no agreement between the State of Washington and the State of Alaska as to the allocation of the New PREMERA shares between the Washington Foundation Shareholder and Alaska Health Foundation on or before receipt of the last of the approvals set forth in Section 4.3 of the Plan of Conversion, or if distribution of the New PREMERA shares to the Washington Foundation Shareholder and Alaska Health Foundation is precluded, New PREMERA, the Washington Foundation Shareholder, and Alaska Health Foundation and the Unallocated Shares Escrow Agent shall execute the Unallocated Shares Escrow Agreement.

- Step 24. New PREMERA, New PBC, the Washington Foundation Shareholder, and Alaska Health Foundation-shall execute and deliver the License Agreement.
- Step 25. New PREMERA and the Escrow Agent shall execute and deliver the Excess Shares Escrow Agreement.
- Step 26. New PREMERA and PBC-AK shall execute and deliver their Guaranty Agreement.
- Step 27. New PREMERA and New PBC shall execute and deliver their Guaranty Agreement.

**Articles of Incorporation of New PREMERA**  
**Exhibit B-1 to the Amended Form A**

the foregoing, in the event that an Independent Board Majority shall have approved an acquisition of outstanding Capital Stock (as defined in **Article IV, Section 1** hereof) of the Corporation, prior to the time such acquisition shall occur, which would otherwise render a Person a Major Participant and such Person (a) shall not have made any subsequent acquisition of outstanding Capital Stock of the Corporation not approved by an Independent Board Majority and (b) shall not have subsequently taken any of the actions specified in the preceding sentence without the prior approval of an Independent Board Majority, then such Person shall not be deemed a Major Participant; provided that the Washington Foundation Shareholder, the Alaska Health Foundation and their affiliates and associates shall always be deemed Major Participants notwithstanding any approval of any acquisition of Capital Stock of the Corporation or any other development or fact of any kind. In the event there shall be any question as to whether a particular Person is a Major Participant, the determination of an Independent Board Majority shall be binding upon all parties concerned.

#### **Section 5      Nomination of Directors by Shareholders.**

(a) Shareholders shall only be entitled to nominate individuals to be elected to the Board of Directors if such individuals are “**Qualified Candidates**” as set forth in this **Section 5** and if such individuals are otherwise qualified to be elected and to serve as directors pursuant to these Articles of Incorporation and the Bylaws of the Corporation. In addition, shareholders may not nominate an individual to be elected to the Board of Directors if the nominee’s candidacy or election would violate state or federal law or the rules of a national securities exchange or association applicable to the Corporation (other than director independence standards that require a subjective determination by the board of directors or a board committee as to the nominee’s independence).

(b) In order for an individual to be a “**Qualified Candidate**,” all of the following requirements must be satisfied:

(1) The nomination must be made for an election to be held at an annual meeting of shareholders or a special meeting of shareholders in which the Board of Directors has determined that candidates will be elected by the issued and outstanding shares of the Corporation’s Common Stock to one or more positions on the Board of Directors.

(2) The individual must be nominated by a shareholder or shareholder group who (i) shall have been the Beneficially Owner (individually or in the aggregate) of more than 5% of the Corporation’s Capital Stock for a continuous period of at least two years as of the date of nomination and must intend to continue to Beneficially Own such shares through the date of the meeting of shares entitled to be voted at that meeting for the election of directors, (ii) is eligible to report Beneficial Ownership on Schedule 13G, rather than 13D, and must have filed a Schedule 13G or an amendment to Schedule 13G reporting its beneficial ownership as a passive or institutional investor (or group) on or before the date that it submits the nomination to the Corporation and (iii) has not entered into an agreement with the Corporation the terms of which prohibit the shareholder from nominating candidates to be directors. Such qualified nominating shareholder or shareholder group shall be referred to herein as the “**Nominating Shareholder**”.

**Bylaws of New Premera Corp.**  
**Exhibit B-2 to the Amended Form A**

organization that sells or delivers health care services. This Section is designed to reflect and be consistent with the rules of the Blue Cross Blue Shield Association ("BCBSA"). If the limitations under the BCBSA rules are amended, this Section shall be construed to permit Board of Director representation to the full extent permitted under such rules, as so amended.

**Section 4 Independent Directors.** A majority of the Board of Directors shall also be "Independent Directors" as such term is defined below. To qualify as an "**Independent Director**," the members of the Board of Directors must affirmatively determine that the director has no material relationship with the Corporation (either directly or as a partner, shareholder or officer of an organization that has a relationship with the Corporation). In addition to the determination above, members of the Board of Directors shall be considered "Independent Directors" if they are not, or have not been, engaged in any of the following relationships:

(a) A director who is or has been an employee or executive officer of the Corporation or the Blue Cross and Blue Shield Association or any of its affiliates, at any time during the past five (5) years.

(b) A director who is, or at any time during the past five (5) years has been, affiliated with or employed by a present or former auditor of the Corporation or any of its affiliates.

(c) A director who currently is employed, or at any time during any of the past three (3) years was employed, as an executive of another company where any of the Corporation's present executives serves on that company's compensation committee.

(d) A director who is an "affiliate" (as defined below) of the Corporation or any subsidiary.

(e) A director who receives, or has at any time during the past five (5) years received, more than \$100,000 per year in direct compensation from the Corporation, other than director and committee fees, pension or other forms of deferred compensation for prior service (provided such compensation is not contingent in any way on continued service), compensation for service as a former CEO or chairman or compensation received by an immediate family member for service as an employee of the Corporation at a level below executive officer.

(f) A director who is currently employed as an employee or executive officer of another company (A) that accounts for at least two (2) percent or \$1 million, whichever is greater, of the Corporation's consolidated gross revenues, or (B) for which the Corporation accounts for at least two (2) percent or \$1 million, whichever is greater of such other company's consolidated gross revenues.

(g) A director who has an immediate family member that fits in any of the foregoing categories currently or at any time during the past five (5) years. For purposes of this Section 3.04 (b), the term "immediate family member" is defined to include a director's spouse, parents, children, siblings, in-laws, and anyone (other than domestic employees) sharing such director's residence.

(h) A director who would not qualify as independent under any applicable federal securities laws and regulations or listing requirements or rules of any national securities exchange or national association on which the Corporation's securities are listed.

In addition to the requirements set forth in this Section 4, the composition and qualifications of the Corporation's Board of Directors shall comply with the requirements set forth in Article III, Section 4 of the Articles of Incorporation.

For purposes of these Bylaws, the terms "affiliate" of, or a person "affiliated with", a specified person, means a person that directly, or indirectly through one or more intermediaries, controls or is controlled by, or is under common control with, the Corporation or any subsidiary. A person will be deemed not to be in control of the Corporation if the person (A) is not the beneficial owner, directly or indirectly, of 10% or more of any class of voting equity securities of the Corporation; and (B) is not an executive officer of the Corporation. A director, executive officer, partner, member, principal or designee of an affiliate (other than a wholly-owned subsidiary or parent company of the Corporation) will be deemed to be an affiliate.

**Section 5 Number; Classes; Term; Initial Directors.** The number, classes, terms and names of the initial directors shall be as set forth in Article III, Section 3, of the Articles of Incorporation.

**Section 6 Board of Directors' Power to Alter the Number of Directors and the Size of Classes.** The Board of Directors shall have the power (within the limitations prescribed by the Articles of Incorporation) by a resolution adopted by an Independent Board Majority (as defined in Article III, Section 4(b) of the Articles of Incorporation) at the time of such adoption to alter at any time and from time to time (i) the total number of directorship positions on the Board of Directors, and (ii) the number of directorship positions in any of the three classes of directors established by the Articles of Incorporation. Except as otherwise expressly provided in the Articles of Incorporation, from the adoption of any particular resolution in the manner provided in the preceding sentence until the adoption in the manner prescribed by the preceding sentence of any subsequent resolution altering the results of the particular resolution, (i) the total number of directorship positions on the Board of Directors shall be equal to the number specified in the particular resolution, and (ii) the number of directorship positions in each of the three classes of directors established by the Articles of Incorporation shall be the number established in the particular resolution.

the power and authority of the Board of Directors in the management of the business and affairs of the Corporation and may transact such business of the Corporation as may be required between meetings of the Board of Directors and as may, from time to time, be requested by the Board of Directors, subject to the limitation on the authority of committees contained in Article III, Section 1 of these Bylaws and in the Act and except in regard to matters that have been specifically delegated to another committee of the Board of Directors or which are required to be addressed by a specific committee of the Board of Directors by applicable law or national stock exchange rule or listing requirement.

(3) *Committee Meetings.* The Executive Committee shall meet from time to time on the call of the Chair of the Board or the President and Chief Executive Officer or of any two (2) or more members of the Executive Committee, such meetings to be held at the date, time and place as may be designated in the notice of the meeting given by the person so authorized by these Bylaws. Notice of the date, time and place of each meeting of the Executive Committee shall be given to each member of the Executive Committee either in person, by mail, by facsimile or similar electronic means, or by telephone, not less than two (2) business days prior to the meeting; such notice need not state the purpose or purposes of the meeting.

(4) *Chair of the Committee.* The Chair of the Board shall be the chair of the Executive Committee, provided that the Chair of the Board does not hold the position of Chief Executive Officer of the Corporation. In the event that the Chair of the Board of Directors holds the position of Chief Executive Officer of the Corporation, the chair of the Executive Committee shall be a director, other than the Chief Executive Officer.

(5) *Quorum.* A majority of the members of the Executive Committee shall constitute a quorum, provided any action to be taken by the Executive Committee shall require either (i) the presence of at least a majority of the members of the Executive Committee other than the President and Chief Executive Officer and the affirmative vote of a majority of the members present at such meeting and entitled to vote on such matter, or (ii) a unanimous vote of the members entitled to vote on such matter and who are present at a meeting at which a quorum is present.

(6) *Minutes and Reports to the Board.* The Executive Committee shall keep regular minutes of its meetings and proceedings. All business transacted by the Executive Committee shall be reported to the Board of Directors at the next regular meeting of the Board of Directors or at a special meeting called for that purpose and shall be subject to ratification, revision or alteration by two-thirds vote of the Board of Directors, provided that no rights of third parties shall be affected by any such revision or alteration.

(b) Nominating and Governance Committee.

(1) *Membership.* Membership on the Nominating and Governance Committee shall consist of not less than four (4) members of the Board of Directors, none of whom shall be employees of the Corporation or any of its Subsidiaries. The Chair of the Board shall be a member of the Nominating and Governance Committee if such person does not also

hold the position of Chief Executive Officer of the Corporation. In addition, each member must qualify as an Independent Director as such term is defined in Article II, Section 4 above.

(2) *Powers and Duties.* The Nominating and Governance Committee shall:

(A) Oversee any and all governance matters affecting the Corporation's Board of Directors. This is to specifically include a review of the Corporation's governance documents whenever appropriate, but at least on a biennial basis, and also to include other matters that may from time to time be referred to the Committee by the Board of Directors.

(B) Nominate candidates to serve on the Corporation's Board of Directors, ensure that the Board of Directors and its committees are comprised of individuals who have strength of character, an inquiring and independent mind, practical wisdom, mature judgment and a strong commitment to the interests and integrity of the Corporation and who are qualified to serve on the Board of Directors or its committees, as the case may be, pursuant to the corporate governance standards set forth under regulatory requirements or approved by the Board of Directors.

(C) Develop and recommend to the Board of Directors guidelines and criteria to determine the qualifications of directors, and to review such guidelines and criteria annually.

(D) Review the qualifications of and recommend to the Board of Directors nominees for directors to be elected by the Board of Directors to fill vacancies and newly created directorships.

(E) Consider and, when appropriate, make recommendations to the Board of Directors concerning the size and composition of the Board of Directors at least every three (3) years.

(F) Annually bring to the Board of Directors a recommendation for the composition of the committees; the Committee should continually address rotation of members of the Board of Directors onto all committees; the chairperson of a committee should be limited to three (3) years with the desirability of having a former chairperson leaving that committee within one (1) year of serving as chair.

(G) Develop and recommend appropriate processes to enable the Board of Directors as a whole to review its effectiveness, as well as the effectiveness of its individual members.

(H) Ensure that management and the Board of Directors have plans in place to provide for both emergency and ongoing succession of key management positions.

(I) Perform such other governance-related functions as may be specified in the Nominating and Governance Committee Charter.

**Transfer, Grant and Loan Agreement**  
**Exhibit G-3 to the Amended Form A**

## TRANSFER, GRANT AND LOAN AGREEMENT

This Transfer, Grant and Loan Agreement (the "Agreement") is made and entered into by and among PREMERA, a Washington nonprofit miscellaneous corporation ("PREMERA"); Premera Blue Cross, a Washington nonprofit corporation ("PBC"); [New PREMERA Corp.], a Washington corporation ("New PREMERA Corp."); and [Washington Foundation Shareholder], a Washington nonprofit corporation ("Washington Foundation Shareholder"), and [Alaska Health Foundation], an Alaska nonprofit corporation ("Alaska Health Foundation") (individually a "Foundation" and collectively, the "Foundations").

### RECITALS

WHEREAS, the Members of PREMERA (the "Members") adopted amendments to PREMERA's articles of incorporation that, among other things, provide that the Foundations will be PREMERA's sole voting members (the "Amendments"); and

WHEREAS, the Members adopted the Amendments in anticipation of the execution of (a) the transaction documents set forth in Exhibit A, which is attached hereto and incorporated by this reference herein (collectively, the "Transaction Documents"); (b) the Acknowledgements and Consents of the Foundations, executed on \_\_\_\_\_, 2004 (the "Consents"); and (c) this Agreement; and

WHEREAS, the Foundations' membership rights pursuant to the terms of the Amendments include the right, subject to certain conditions, to receive PREMERA's assets upon consummation of a series of transactions contemplated by the Plan of Conversion on its dissolution; and

WHEREAS, contemporaneously with the execution of this Agreement, PREMERA will take all actions and execute all documents necessary to effect its dissolution in connection with and as part of the Plan of Conversion; and

WHEREAS, as a result of such series of transactions as contemplated in the Plan of Conversion including the dissolution of PREMERA, each Foundation will acquire a share of PREMERA's assets, which in the aggregate consist of [ ] shares of New PREMERA Corp.'s common stock, no par value per share (the "Common Stock"), and the Washington Foundation Shareholder will receive one share of Class B Common Stock (the "Class B Common Stock"), representing collectively 100% of the issued and outstanding shares of the Common Stock at the time of PREMERA's dissolution; and

WHEREAS, subject to each Foundation's Articles of Incorporation, Bylaws and the Transaction Documents, each of Alaska Health Foundation and the Washington Foundation Shareholder have power to manage, control and dispose their respective shares of the Common Stock; and

WHEREAS, each Foundation acknowledges, pursuant to the Consent and Plan of Distribution, that any assets each receives on PREMERA's dissolution are subject to certain limitations;

WHEREAS, each Foundation hereby acknowledges that receipt of the Common Stock is contingent upon its acknowledgement that the Common Stock and any income and proceeds generated thereon, as invested and reinvested, are subject to the conditions, restrictions and limitations on future use contained herein; and

WHEREAS, PBC has agreed to make certain grants and loans to the Foundations to assist with Foundation expenses prior to their receipt and sale of the Common Stock;

NOW, THEREFORE, in consideration of the foregoing and the mutual covenants contained herein and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

## ARTICLE I

### COMMON STOCK, COMMON STOCK PROCEEDS EXPENDITURE OF PROCEEDS

Section 1.01. Receipt, Holding, and Disposition of Common Stock. The Foundations will receive their respective Common Stock on dissolution of PREMERA as part of the Plan of Conversion. In addition, the Washington Foundation Shareholder will receive the Class B Common Stock upon dissolution of PREMERA as part of the Plan of Conversion. Each of the Foundations has certain obligations to divest the Common Stock over time as provided in the Voting Trust and Divestiture Agreement between each Foundation, New PREMERA, and the Trustee thereunder. Other than as provided in the divestiture provisions of such Voting Trust and Divestiture Agreements, there is no other obligation as to the timing of decisions to sell the Common Stock and the transfer of the Common Stock to the Foundations is made with the understanding that the Foundations and their respective boards of directors are not required to take actions and make decisions as to the timing and amounts of sales of the Common Stock to comply with diversification provisions in RCW 11.100.020.

Section 1.02. Permissible Purposes. Each Foundation hereby acknowledges and agrees that the proceeds from the sale of the Common Stock and any amounts generated by such proceeds, including without limitation investment income as such proceeds are invested and reinvested ("Common Stock Proceeds") may be expended, transferred or used solely to promote the health of the residents of the States of Washington and Alaska by making grants or gifts to one or more nonprofit organizations recognized as exempt from federal income taxation under Section 501(c)(3a) of the Internal Revenue Code of 1986, as amended (the "Code") and which organizations commit in writing to hold and use such gifts and grants exclusively to accomplish the purposes described in the subsections below; *provided, however*, that in no event will Common Stock Proceeds be used for the Impermissible Purposes set out in Section 1.03 of this Agreement.

reimbursement of reasonable out-of-pocket expenses incurred by the Washington Foundation Shareholder and the Alaska Health Foundation, respectively (which could include possible lobbying activities allowed under section 1.03(a)) pursuant to the Budgets (as defined below) (collectively, the "Grants"); and (ii) loan the Washington Foundation and the Alaska Foundation up to Two Hundred Fifty Thousand Dollars (\$250,000) each in one or more installments during the Pre-IPO Period (the "Loans") to further provide for such expenses. As a condition precedent to PBC making the Grant and the Loan to each Foundation, each Foundation shall submit to PBC and New PREMERA Corp. a proposed operating budget (the "Budgets") for the period from the Approval Date until the first offering in which securities of New PREMERA Corp. are sold to an underwriter for reoffering to the public pursuant to an effective registration statement under the Securities Act of 1933, as amended (the "IPO" and such period from the Approval Date to the IPO, the "Pre-IPO Period"), such Budgets to include anticipated operating expenses for the Pre-IPO Period, including, without limitation, administration fees, legal fees, accounting and financial advisory fees, office expenses, expenses related to the maintenance of personnel (including the board of directors, if compensated), and possible lobbying activity expenses if allowed under section 1.03(a) (collectively, the "Operating Expenses") of each Foundation. Each Loan shall be evidenced by a promissory note from the respective Foundation in favor of PBC or its assigns in the amount of the Loan in the form of Exhibits B-1 and B-2, respectively, attached hereto (the "Notes"). The Loans shall bear no interest and shall be non-recourse, payable solely from the proceeds each Foundation receives by selling shares of New PREMERA Corp. Common Stock in the IPO. The Notes shall be repaid concurrently with the closing of the IPO (or, if the Foundation does not participate in the IPO as a selling shareholder, the first offering in which the Foundation participates as a selling shareholder) by deduction of the principal outstanding under each Note from the amount of proceeds of such IPO (or subsequent offering) that would otherwise be payable to such Foundation as a selling shareholder. Each Foundation also shall transfer to New PREMERA Corp. any Grant funds not used for expenses incurred pursuant to such Foundation's Budget.

### ARTICLE III

#### OTHER CONDITIONS

Section 3.01. No Amendments. Each Foundation acknowledges the importance of the structure and content of its governing documents to the nature of its receipt of proceeds from the liquidation of PREMERA and accordingly each Foundation agrees that so long as it holds the Common Stock or the proceeds of sale thereof, it shall not (i) amend, alter or repeal its Articles of Incorporation (other than to change its Registered Office or Agent) or its Bylaws without (A) the affirmative vote of three-fourths (3/4) of the members of its Board of Directors then in office and (B) advance written approval of the Alaska or Washington Attorney General, as applicable; or (ii) amend, alter or repeal Articles of Incorporation to be inconsistent with the purpose of promoting the health of the residents of the State of Washington or Alaska, as applicable.

Section 3.02. Distribution of Common Stock Proceeds Requirements. Before either Foundation distributes any Common Stock Proceeds to any organization exempt from taxation under Section 501(c)(3) of the Code (collectively, "Charitable Organizations"), each Foundation will enter into a grant agreement with the applicable Charitable Organization that:

(a) requires that such proceeds received from the Foundation be expended, pledged, transferred and used only in furtherance of the purposes set forth in Section 1.02 of this Agreement and subject to the limitations set forth in Section 1.03 of this Agreement;

(b) provides the Foundation with the right to injunctive relief to enforce its rights under such agreement;

(c) recognizes that the Alaska and Washington Attorney General, as applicable, have a right to pursue injunctive relief and that New PREMIERA Corp. is a third-party beneficiary and has a right to pursue injunctive relief to enforce the terms of such agreement;

(d) requires such Charitable Organization to provide the Foundation at least annually with a summary of the charitable programs and activities supported by the Common Stock Proceeds;

(e) recognizes the requirement that the Charitable Organization maintain its Section 501(e)(3)a status under the Code; and

(f) provides the Foundation with a right to audit its Charitable Organization activities as consistent with the grant agreement.

Section 3.03. Record Maintenance and Inspection. Each Foundation agrees to maintain adequate records to enable expenditure of the proceeds from the sale of the Common Stock and distribution of proceeds to the Charitable Organizations to be easily confirmed. Each Foundation will make its books and records available for inspection by the Alaska and Washington Attorneys General respectively at reasonable times and permit the Alaska and Washington Attorneys General to monitor and conduct an evaluation of operations of the Alaska Health Foundation and Washington Foundation Shareholder, respectively, under this Agreement.

Section 3.04 Distribution on Dissolution. Upon the winding up and dissolution of either of the Foundations, the assets of such Foundation remaining after payment of, or provision for payment of, all debts and liabilities of such Foundation, shall be distributed as follows:

(a) Any amounts remaining after paying or providing for all liabilities in the Alaska Health Foundation shall be distributed to one or more nonprofit corporations located in the State of Alaska recognized as exempt under Section 501(c)(3) of the Code, and approved by the Alaska Attorney General for use exclusively to accomplish the purposes described in Section 1.02.2 of this Agreement and subject to the limitations described in Section 1.03 of this Agreement.

(b) Any amounts remaining after paying or providing for all liabilities in the Washington Foundation Shareholder shall be distributed to one or more nonprofit corporations located in the State of Washington recognized as exempt under Section 501(c)(3) of the Code, and approved by the Washington Attorney General for use exclusively to accomplish the

purposes described in Section 1.02.1 of this Agreement and subject to the limitations described in Section 1.03 of this Agreement.

## **ARTICLE IV**

### **FOUNDATION REPRESENTATIONS AND WARRANTIES**

Each Foundation hereby represents and warrants to PREMERA and [New PREMERA Corp.] that: as of the Closing Date (as defined in the Plan of Conversion):

(a) the Foundation is a nonprofit corporation duly organized and validly existing under the laws of the State of Washington and State of Alaska, respectively;

(b) the Foundation has the corporate power to execute, deliver and perform its obligations under this Agreement;

(c) the Foundation has authorized the execution, delivery and performance of its obligations under this Agreement by all necessary corporate action;

(d) the Foundation has duly executed and delivered this Agreement;

(e) the execution and delivery by the Foundation of this Agreement and the performance by the Foundation of its obligations hereunder (i) do not violate its articles of incorporation or bylaws and (ii) do not breach or result in a default under any agreement to which the Foundation is a party;

(f) the Foundation has not (i) amended, altered or repealed its Articles of Incorporation; or (ii) amended, altered or repealed its Bylaws except as permitted in this Agreement; and

(g) as of the Effective Date of this Agreement, the Foundation is not in breach of its obligations hereunder.

## **ARTICLE V**

### **TERM AND TERMINATION**

This Agreement shall be effective upon the Approval Date (the "Effective Date") and shall terminate as to each Foundation when such Foundation ceases to own any Common Stock and has distributed all of the Common Stock Proceeds; provided that Sections 1.02 and 1.03, Sections 3.01 through 3.04 and Section 6.05 of this Agreement shall survive termination of this Agreement. Upon the occurrence of the foregoing, such Foundation agrees to provide, pursuant

**AK Voting Trust and Divestiture Agreement**  
**Exhibit G-4 to the Amended Form A.**

shares so withdrawn to be registered in the name of Beneficiary or its nominee before being so withdrawn. For purposes of calculating the Voting Ownership Limit under this Section 3.02, an Additional Issuance of securities exercisable, convertible or exchangeable into Common Stock will be included in the calculation of the voting power of all shares of issued and outstanding Capital Stock at the time such shares are exercised, converted or exchanged for Common Stock.

## ARTICLE IV

### TRUSTEE'S POWERS AND DUTIES

Section 4.01. Limits on Trustee's Powers. The Trustee shall have only the powers set forth in this Agreement. It is expressly understood and agreed by the parties hereto that under no circumstances shall the Trustee be personally liable for the payment of any indebtedness or expenses of this Agreement or be liable for the breach or failure of any obligation, representation, warranty, or covenant made or undertaken by the Trustee under this Agreement, except as set forth in this Agreement.

Section 4.02. Right to Vote. With respect to all shares of Capital Stock held in the Voting Trust, the Trustee shall have the exclusive and absolute right in respect of such shares of Capital Stock to vote, assent or consent such shares of Capital Stock at all times during the term of this Agreement, subject to Section 4.03 hereof.

Section 4.03. Voting on Particular Matters. In exercising the Trustee's powers and duties under this Agreement, subject to Section 4.04 hereof, the Trustee shall at all times vote, assent or consent all shares of Capital Stock held in the Voting Trust as follows:

(a) if the matter concerned is the election of directors of the Company, the Trustee shall vote, assent or consent the whole number of shares of Capital Stock held by the Voting Trust (x) in favor of each nominee to the Board of Directors whose nomination has been approved by an Independent Board Majority and vote against any candidate for the Board of Directors for whom no competing candidate has been nominated, selected or approved by an Independent Board Majority, and (y) if the nomination of a nominee has not been approved by an Independent Board Majority, in favor of such nominee if such nominee has been nominated by the Board of Directors in the manner provided in Section 5.03(b)(i) hereof;

(b) unless such action is initiated by or with the consent of an Independent Board Majority, the Trustee shall vote against removal of any director of the Company;

(c) if the matter concerned is (x) an employee compensation plan (other than the approval of the Initial Equity Incentive Plan, as to which all shares of Capital Stock held by the Voting Trust or by the Beneficiary outside the Voting Trust shall be voted in accordance with Section 4.03(e) below; or (i) a subsequent amendment to said Initial Equity Incentive Plan or, (ii) any new Stock-Based Program that would be effective during the Stock Restriction Period,

~~provided, that~~ (iii) any ~~such~~ new Stock-Based Program shall ~~not have been~~ that would be effective after the Stock Restriction Period but that is submitted to a shareholder vote for approval prior to the date which is twelve (12) months prior to the end of the Stock Restriction Period, as to which all shares of Capital Stock held by the Voting Trust or by the Beneficiary outside the Voting Trust shall be voted in accordance with Section 4.03(d) and 4.03(e) below for which stockholder approval is sought or (y) a precatory stockholder proposal (*i.e.*, advisory proposals made by a stockholder of the Company pursuant to Rule 14a-8 promulgated under the Exchange Act (or in any successor provision) that merely recommended or requested that the Board of Directors or the Company take certain action), the Trustee shall vote all Capital Stock held by the Voting Trust in the same proportions as the shares voted by all holders of Capital Stock other than shares voted by (i) the Voting Trust, (ii) the Beneficiary, (iii) the ~~Washington Alaska Health~~ Foundation Shareholder and (iv) directors, officers, trustees of any employee benefit plans of the Company and other Affiliates of the Company (whether acting in their individual ownership or fiduciary capacities or pursuant to a discretionary proxy (other than any revocable proxy given by a stockholder other than a director, officer, trustee of any Company employee benefit plan or other Affiliate of the Company in response to a solicitation of proxies by the Board of Directors of the Company) or other discretionary delegation of the right to direct the voting of another stockholder's shares of Capital Stock);

(d) if the matter concerned is an Approved Change of Control Proposal or a subsequent amendment to the Initial Equity Incentive Plan, the Trustee shall vote all Capital Stock held by the Voting Trust as directed by the Beneficiary, in its sole discretion;

(e) ~~(d) if the matter concerned is an Approved Change of Control Proposal, a subsequent amendment to the Initial Equity Incentive Plan or if the matter concerned is any new Stock-Based Program that: (i) would be effective during the Stock Restriction Period, provided, that any or (ii) would be effective after the Stock Restriction Period and such new Stock-Based Program shall not have been~~ is submitted to a shareholder vote for approval prior to the date which that is twelve (12) months prior to the end of the Stock Restriction Period, the Trustee shall vote all Capital Stock held by the Voting Trust as directed by the Beneficiary, in its sole discretion; and

(f) ~~(e) to the extent not otherwise covered by Section 4.03(a), Section 4.03(b), Section 4.03(c), Section 4.03(d) or Section 4.03(de) hereof, the Trustee shall vote in accordance with the recommendation of the Independent Board Majority.~~

taking any particular action as a result of such consultation. The Beneficiary shall comply with the same confidentiality and non-disclosure obligations that apply to directors and officers of the Company and with the provisions of the Confidentiality Agreement with respect to all information obtained by the Beneficiary in connection with any such consultation. Nothing in this Agreement shall be construed to limit the rights of the Beneficiary as a shareholder of the Company to communicate with the Board of Directors of the Company regarding Acquisition Proposals or Change of Control Proposals or, except as otherwise provided in Section 5.07 hereof, any other matter pertaining to the Company. The Company and the Beneficiary shall keep confidential the contents of all such communications from the Beneficiary, provided that either party may disclose the contents of such communications if required by law, subject to the Confidentiality Agreement.

## **ARTICLE VII**

### **AGREEMENT TO DIVEST SHARES OF CAPITAL STOCK**

Section 7.01. Sale of Beneficiary's Capital Stock by First Anniversary. (a) Subject to the Beneficiary's obligations in Section 7.01(b), Section 7.02, Section 7.03 and Section 7.04, the Beneficiary will, to the extent consistent with its duties and obligations and purposes and taking into account market conditions, reduce its Beneficial Ownership of Capital Stock in a prudent and reasonably prompt manner. The Company will likewise use its commercially reasonable efforts, in response to reasonable requests from the Beneficiary, and subject to the terms of the Registration Rights Agreement, to facilitate the Beneficiary's reduction in its Beneficial Ownership of Capital Stock.

(b) The Beneficiary hereby covenants and agrees that it shall sell, convey, or otherwise dispose of shares of Capital Stock (so that the Beneficiary is no longer a Beneficial Owner of such shares of Capital Stock) so that the Beneficiary and the Washington Foundation Shareholder together Beneficially Own less than eighty percent (80%) of the issued and outstanding shares of each class of Capital Stock (other than Class B Common Stock) on or prior to the One Year Divestiture Deadline. Any such disposition shall comply with the terms of this Agreement, the Registration Rights Agreement, the Articles of Incorporation, and the Bylaws. The requirements under this Section 7.01(b) shall be eliminated only if the Company receives approval from the BCBSA for such elimination.

Section 7.02. Sale of Beneficiary's Capital Stock by Third Anniversary. The Beneficiary hereby covenants and agrees that it shall sell, convey, or otherwise dispose of shares of Capital Stock (so that the Beneficiary is no longer a Beneficial Owner of such shares of Capital Stock) so that the Beneficiary and the Washington Foundation Shareholder together Beneficially Own less than fifty percent (50%) of the issued and outstanding shares of each class of Capital Stock (other than Class B Common Stock) on or prior to the Three Year Divestiture Deadline. Any

such disposition shall comply with the terms of this Agreement, the Registration Rights Agreement, the Articles of Incorporation, and the Bylaws.

Section 7.03. Sale of Beneficiary's Capital Stock by Fifth Anniversary. The Beneficiary hereby covenants and agrees that it shall sell, convey or otherwise dispose of shares of Capital Stock (so that the Beneficiary is no longer a Beneficial Owner of such shares of Capital Stock) so that the Beneficiary and the Washington Foundation Shareholder together Beneficially Own less than twenty percent (20%) of the issued and outstanding shares of each class of Capital Stock (other than Class B Common Stock) on or prior to the Five Year Divestiture Deadline. Any such disposition shall comply with the terms of this Agreement, the Registration Rights Agreement, the Articles of Incorporation, and the Bylaws.

Section 7.04. Sale of Beneficiary's Capital Stock by Tenth Anniversary. The Beneficiary hereby covenants and agrees that it shall sell, convey or otherwise dispose of shares of Capital Stock (so that the Beneficiary is no longer a Beneficial Owner of such shares of Capital Stock) so that the Beneficiary and the Washington Foundation Shareholder together Beneficially Own less than five percent (5%) of the issued and outstanding shares of each class of Capital Stock ~~(other than Class B Common Stock)~~ on or prior to the Ten Year Divestiture Deadline. Any such disposition shall comply with the terms of this Agreement, the Registration Rights Agreement, the Articles of Incorporation, and the Bylaws.

Section 7.05. Extension of Divestiture Deadlines Sought by Beneficiary. Notwithstanding Section 7.01, Section 7.02, Section 7.03 or Section 7.04 hereof, the Company shall extend a Divestiture Deadline if (i) the Beneficiary makes a good faith and reasonable determination (and provides the reasons therefor) that compliance with Section 7.01, Section 7.02, Section 7.03 or Section 7.04, hereof, as the case may be, would have a material adverse effect on the Beneficiary's ability to maximize the value of its assets or would be in conflict with its legal or fiduciary duties, (ii) the Beneficiary advises the Company of such determination in writing (and provides the reasons therefor) no later than ninety (90) days prior to the Divestiture Deadline and makes a reasonable request for an extension of the Divestiture Deadline, and (iii) the Company receives written confirmation from the BCBSA that the extension of the Divestiture Deadline, requested by the Beneficiary would not cause a violation of the license agreements governing the Company's use of the Marks. The Company shall not oppose the Beneficiary's request for an extension of a Divestiture Deadline, and shall take reasonable steps, as reasonably requested by the Beneficiary, to assist the Beneficiary in its efforts to obtain an extension of a Divestiture Deadline. The Beneficiary acknowledges that, notwithstanding the scope or degree of assistance provided by the Company, the BCBSA shall have the sole and absolute authority and discretion to determine whether to consent to an extension of a Divestiture Deadline, but shall have no obligation to grant such consent, and that in no event shall the Company have any liability to the Beneficiary or any other Person in the event that the BCBSA shall determine to deny any such extension request.

**WA Voting Trust and Divestiture Agreement**  
**Exhibit G-4 to the Amended Form A**

## ARTICLE IV

### TRUSTEE'S POWERS AND DUTIES

Section 4.01. Limits on Trustee's Powers. The Trustee shall have only the powers set forth in this Agreement. It is expressly understood and agreed by the parties hereto that under no circumstances shall the Trustee be personally liable for the payment of any indebtedness or expenses of this Agreement or be liable for the breach or failure of any obligation, representation, warranty, or covenant made or undertaken by the Trustee under this Agreement, except as set forth in this Agreement.

Section 4.02. Right to Vote. With respect to all shares of Capital Stock held in the Voting Trust, the Trustee shall have the exclusive and absolute right in respect of such shares of Capital Stock to vote, assent or consent such shares of Capital Stock at all times during the term of this Agreement, subject to Section 4.03 hereof.

Section 4.03. Voting on Particular Matters. In exercising the Trustee's powers and duties under this Agreement, subject to Section 4.04 hereof, the Trustee shall at all times vote, assent or consent all shares of Capital Stock held in the Voting Trust as follows:

(a) if the matter concerned is the election of directors of the Company, the Trustee shall vote, assent or consent the whole number of shares of Capital Stock held by the Voting Trust (x) in favor of each nominee to the Board of Directors whose nomination has been approved by an Independent Board Majority and vote against any candidate for the Board of Directors for whom no competing candidate has been nominated, selected or approved by an Independent Board Majority, and (y) if the nomination of a nominee has not been approved by an Independent Board Majority, in favor of such nominee if such nominee has been nominated by the Board of Directors in the manner provided in Section 5.03(b)(i) hereof;

(b) unless such action is initiated by or with the consent of an Independent Board Majority, the Trustee shall vote against removal of any director of the Company;

(c) if the matter concerned is (x) an employee compensation plan (other than the approval of the Initial Equity Incentive Plan, as to which all shares of Capital Stock held by the Voting Trust or by the Beneficiary outside the Voting Trust shall be voted in accordance with Section 4.03(e) below; or (i) a subsequent amendment to said Initial Equity Incentive Plan or, (ii) any new Stock-Based Program that would be effective during the Stock Restriction Period, ~~provided, that or (iii) any such new Stock-Based Program shall not have been that would be effective after the Stock Restriction Period but that is~~ submitted to a shareholder vote for approval prior to the date which is twelve (12) months prior to the end of the Stock Restriction Period, as to which all shares of Capital Stock held by the Voting Trust or by the Beneficiary outside the Voting Trust shall be voted in accordance with Section 4.03(d) and 4.03(e) below)

for which stockholder approval is sought or (y) a precatory stockholder proposal (*i.e.*, advisory proposals made by a stockholder of the Company pursuant to Rule 14a-8 promulgated under the Exchange Act (or in any successor provision) that merely recommended or requested that the Board of Directors or the Company take certain action), the Trustee shall vote all Capital Stock held by the Voting Trust in the same proportions as the shares voted by all holders of Capital Stock other than shares voted by (i) the Voting Trust, (ii) the Beneficiary, (iii) the Alaska Health Foundation and (iv) directors, officers, trustees of any employee benefit plans of the Company and other Affiliates of the Company (whether acting in their individual ownership or fiduciary capacities or pursuant to a discretionary proxy (other than any revocable proxy given by a stockholder other than a director, officer, trustee of any Company employee benefit plan or other Affiliate of the Company in response to a solicitation of proxies by the Board of Directors of the Company) or other discretionary delegation of the right to direct the voting of another stockholder's shares of Capital Stock);

(d) if the matter concerned is an Approved Change of Control Proposal or a subsequent amendment to the Initial Equity Incentive Plan, the Trustee shall vote all Capital Stock held by the Voting Trust as directed by the Beneficiary, in its sole discretion;

~~(e) (d) if the matter concerned is an Approved Change of Control Proposal, a subsequent amendment to the Initial Equity Incentive Plan or if the matter concerned is any new Stock-Based Program that: (i) would be effective during the Stock Restriction Period, provided, that any or (ii) would be effective after the Stock Restriction Period and such new Stock-Based Program shall not have been~~ submitted to a shareholder vote for approval prior to the date ~~which that~~ is twelve (12) months prior to the end of the Stock Restriction Period, the Trustee shall vote all Capital Stock held by the Voting Trust as directed by the Beneficiary, in its sole discretion; and

(f) ~~(e)~~ to the extent not otherwise covered by Section 4.03(a), Section 4.03(b), Section 4.03(c), Section 4.03(d) or Section 4.03(~~e~~) hereof, the Trustee shall vote in accordance with the recommendation of the Independent Board Majority.

Section 4.04. Presence at Meetings. The Trustee shall ensure, with respect to the shares of Capital Stock held in the Voting Trust hereunder, that such shares of Capital Stock are counted as being present for the purposes of any quorum required for shareholder action of the Company and, to vote, assent or consent as set forth in this Article IV so long as the Trustee (i) has reasonable notice of the time to vote, assent or consent (and the Trustee shall be deemed to have reasonable notice if it shall receive notice within the time periods under the applicable provisions of the Revised Code of Washington), or (ii) has waived such notice.

Section 4.05. Sales. The Trustee shall have no authority to sell any of the shares of Capital Stock deposited pursuant to the provisions of this Agreement, unless expressly permitted pursuant to the terms hereof. Upon the sale of shares of Capital Stock in accordance with the terms hereof, the Trustee shall deliver or cause to be delivered certificates representing such shares of Capital Stock to the Person entitled thereto.

## ARTICLE VII

### AGREEMENT TO DIVEST SHARES OF CAPITAL STOCK

Section 7.01. Sale of Beneficiary's Capital Stock by First Anniversary. (a) Subject to the Beneficiary's obligations in Section 7.01(b), Section 7.02, Section 7.03 and Section 7.04, the Beneficiary will, to the extent consistent with its duties and obligations and purposes and taking into account market conditions, reduce its Beneficial Ownership of Capital Stock in a prudent and reasonably prompt manner. The Company will likewise use its commercially reasonable efforts, in response to reasonable requests from the Beneficiary, and subject to the terms of the Registration Rights Agreement, to facilitate the Beneficiary's reduction in its Beneficial Ownership of Capital Stock.

(b) The Beneficiary hereby covenants and agrees that it shall sell, convey, or otherwise dispose of shares of Capital Stock (so that the Beneficiary is no longer a Beneficial Owner of such shares of Capital Stock) so that the Beneficiary and the Alaska Health Foundation together Beneficially Own less than eighty percent (80%) of the issued and outstanding shares of each class of Capital Stock (other than Class B Common Stock) on or prior to the One Year Divestiture Deadline. Any such disposition shall comply with the terms of this Agreement, the Registration Rights Agreement, the Articles of Incorporation, and the Bylaws. The requirements under this Section 7.01(b) shall be eliminated only if the Company receives approval from the BCBSA for such elimination.

Section 7.02. Sale of Beneficiary's Capital Stock by Third Anniversary. The Beneficiary hereby covenants and agrees that it shall sell, convey, or otherwise dispose of shares of Capital Stock (so that the Beneficiary is no longer a Beneficial Owner of such shares of Capital Stock) so that the Beneficiary and the Alaska Health Foundation together Beneficially Own less than fifty percent (50%) of the issued and outstanding shares of each class of Capital Stock (other than Class B Common Stock) on or prior to the Three Year Divestiture Deadline. Any such disposition shall comply with the terms of this Agreement, the Registration Rights Agreement, the Articles of Incorporation, and the Bylaws.

Section 7.03. Sale of Beneficiary's Capital Stock by Fifth Anniversary. The Beneficiary hereby covenants and agrees that it shall sell, convey or otherwise dispose of shares of Capital Stock (so that the Beneficiary is no longer a Beneficial Owner of such shares of Capital Stock) so that the Beneficiary and the Alaska Health Foundation together Beneficially Own less than twenty percent (20%) of the issued and outstanding shares of each class of Capital Stock (other than Class B Common Stock) on or prior to the Five Year Divestiture Deadline. Any such disposition shall comply with the terms of this Agreement, the Registration Rights Agreement, the Articles of Incorporation, and the Bylaws.

Section 7.04. Sale of Beneficiary's Capital Stock by Tenth Anniversary. The Beneficiary hereby covenants and agrees that it shall sell, convey or otherwise dispose of shares of Capital Stock (so that the Beneficiary is no longer a Beneficial Owner of such shares of

Capital Stock) so that the Beneficiary and the Alaska Health Foundation together Beneficially Own less than five percent (5%) of the issued and outstanding shares of each class of Capital Stock ~~(other than Class B Common Stock)~~ on or prior to the Ten Year Divestiture Deadline. Any such disposition shall comply with the terms of this Agreement, the Registration Rights Agreement, the Articles of Incorporation, and the Bylaws.

Section 7.05. Extension of Divestiture Deadlines Sought by Beneficiary. Notwithstanding Section 7.01, Section 7.02, Section 7.03 or Section 7.04 hereof, the Company shall extend a Divestiture Deadline if (i) the Beneficiary makes a good faith and reasonable determination (and provides the reasons therefor) that compliance with Section 7.01, Section 7.02, Section 7.03 or Section 7.04, hereof, as the case may be, would have a material adverse effect on the Beneficiary's ability to maximize the value of its assets or would be in conflict with its legal or fiduciary duties, (ii) the Beneficiary advises the Company of such determination in writing (and provides the reasons therefor) no later than ninety (90) days prior to the Divestiture Deadline and makes a reasonable request for an extension of the Divestiture Deadline, and (iii) the Company receives written confirmation from the BCBSA that the extension of the Divestiture Deadline, requested by the Beneficiary would not cause a violation of the license agreements governing the Company's use of the Marks. The Company shall not oppose the Beneficiary's request for an extension of a Divestiture Deadline, and shall take reasonable steps, as reasonably requested by the Beneficiary, to assist the Beneficiary in its efforts to obtain an extension of a Divestiture Deadline. The Beneficiary acknowledges that, notwithstanding the scope or degree of assistance provided by the Company, the BCBSA shall have the sole and absolute authority and discretion to determine whether to consent to an extension of a Divestiture Deadline, but shall have no obligation to grant such consent, and that in no event shall the Company have any liability to the Beneficiary or any other Person in the event that the BCBSA shall determine to deny any such extension request.

Section 7.06. Extension of Divestiture Deadlines Sought by Company. Notwithstanding Section 7.01, Section 7.02, Section 7.03 or Section 7.04 hereof, the Company shall extend a Divestiture Deadline, if (i) the Company makes a good faith determination that compliance with Section 7.01, Section 7.02, Section 7.03 or Section 7.04 hereof, as the case may be, would have an adverse effect on the Company, or any of its shareholders other than the Beneficiary, and (ii) the Company receives written confirmation from BCBSA that the extension of a Divestiture Deadline requested by the Company would not cause a violation of the license agreement governing the Company's use of the Marks. The Beneficiary and the Company acknowledge that the BCBSA shall have the sole and absolute authority and discretion to determine whether to consent to an extension of a Divestiture Deadline, but shall have no obligation to grant such consent, and that in no event shall the Company have any liability to the Beneficiary or any other Person in the event that the BCBSA shall determine to deny any such extension request.

Section 7.07. Failure to Meet Divestiture Deadlines. In the event that the Beneficiary shall fail to meet a Divestiture Deadline, and an extension thereof shall not have been granted pursuant to Section 7.05 or Section 7.06 hereof, or shall fail to meet any extended Divestiture Deadline that may have been granted pursuant to Section 7.05 and Section 7.06 hereof, then within ten (10) Business Days after such deadline, the Company shall provide a list to the